JUDICIAL CONTROL OF UNFAIR CONTRACTS IN ENGLISH AND SCOTS LAW

by

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Ph.D.

UNIVERSITY OF EDINBURGH

1980

I hereby certify that the research for, and the composition of, this Thesis has been undertaken by myself.

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ABSTRACT OF THESIS

This thesis examines the various techniques which the courts have used to control unfair contracts over the last three centuries. The purpose in doing so is twofold: firstly, to demonstrate that such control has been widely exercised despite the "classical" notion that the sole function of the courts is to protect the freedom of the individual will and their duty to give effect to the terms stipulated in the contract regardless of their fairness; secondly, to identify the factors and policy considerations which in each area lead to judicial control.

In Part I the judicially developed techniques of control are discussed and in Part II the discretionary powers of control conferred by statute are looked at. Part III examines briefly the various phases through which judicial controls have gone since the late seventeenth century and concludes that the present state of controls is unsatisfactory, largely because there is, as yet, no consensus about the basis on which such control should proceed. It is suggested that the courts should exercise control whenever a contract is unfair and that the delimitation of what is unfair should proceed by way of identifying "models" of unfairness to fit the different factual settings.

ACKNOWLEDGEMENTS

My interest in the control of unfair contracts was first occasioned by an article on unconscionability in contracts in the 1976 Modern Law Review by Prof. S.M. Waddams. Further reading on the subject brought to my attention a number of articles by Prof. J.P. Dawson in which the same field was explored. These writings have been a constant source of enlightenment to me throughout the writing of this work and have, wherever necessary, been specifically referred to.

I wish to express my gratitude to my supervisors, Mr. M.G. Clarke and Prof. E.M. Clive for their patient and ever ready assistance during the long process of producing this work. I am also indebted to Miss Sturgeon and the staff of the Edinburgh University Law Library and to Dr. Sandy McCall Smith and Mr. Bob Scott for their constant advice and encouragement. A particular debt of gratitude is owed to Mrs. June Wilson for typing the thesis in often trying circumstances.

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INTRODUCTION

"In general unless a contract is vitiated by duress, fraud or mistake its terms will be enforced though unreasonable or even harsh and unconscionable".[1] The view that the courts do not concern themselves with the substantive fairness of a contract and will not grant relief from a contract because its terms are unfair has been repeated in Scots and English law with such regularity and conviction throughout almost two centuries that recent attempts to develop a more open and direct control of unfair contracts have been criticised as contrary to the established principles of contract law.

The idea that substantive unfairness does not affect the validity of a contract emanated largely from the concept of the bilateral consensual agreement, a conception which, although it was known much earlier, gained its greatest significance during the nineteenth century.[2] The "classical" or will theory of contract, as it became known, was the counterpart of philosophical individualism and free market capitalism.[3] Its fundamental purpose was to give effect to the intention of the parties and its governing principle that of private autonomy or freedom of contract. This meant that, with the exception of a few narrow limitations, the law delegated to private individuals the power to effect

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1 Esso Petroleum Co. Ltd. v. Harper's Garage (Stourport) Ltd. /1968/ A.C. 269, 295.

2 See, generally, M.J. Horwitz, The Historical Foundations of Modern Contract Law (1974) 87 Harv.L.Rev. 917. Cf. A.W.B. Simpson, The Horwitz Thesis and the History of Contracts (1979) 46 U.Chi. L.Rev. 533.

3 See, generally, the account of the rise and development of the classical theory of contract in Kessler and Gilmore, Contracts, 2-14.

such changes in their legal relations as they wished.[1] Although the legal system provided the apparatus or framework, the law which the parties created within that framework was of their own making. The role of the courts within this scheme was, in theory, strictly limited to distinguishing cases of true consent from those where it was defective.[2] Interrelated with the will theory of contract was the idea that things have no intrinsic value.[3] It followed from a combination of these theories that the fairness of an exchange could not be judged ab extra.

> /I/t is the consent of the parties alone, that fixes the just price of any thing, without reference to the nature of things themselves, or to their intrinsic value.[4]

The classical theory presupposed that the contractual parties would be free men of sound judgment, acting rationally and with their eyes open, and that by bargaining a fair result would be reached.

Since the rise of the classical theory of contract two fundamental changes have taken place.[5] In the first place, the majority of contracts concluded today are not individually negotiated, but are in standard form:[6] a party is presented with a set of terms prepared in

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1 Ibid., page 3, footnote 7.

2 Cheshire and Fifoot, Law of Contract, 13.

3 Horwitz, op.cit., 918.

4 Powell, Essay on the Law of Contracts, 229.

5 See, generally, Friedmann, Law in a Changing Society, 119-160; Atiyah, The Rise and Fall of Freedom of Contract, especially 571-715.

6 The literature on standard form contracts is vast. See, for example, N. Isaacs, The Standardization of Contracts (1917) 27 Yale L.J. 34; Prausnitz, The Standardization of Commercial Contracts in English and Continental Law, reviewed by K.N. Llewellyn, (1939) 52 Harv.L.Rev.700;

advance and used in all like transactions which he either has to accept or reject in toto. Standardized contracts have great commercial utility; for example they save time and facilitate a rational allocation of risk. However, while the use of standardized contracts leaves a party free to decide whether to enter into a contract or not, it deprives him of the freedom to co-determine its content. The exclusive power to determine the terms of a standard form contract resides in the form offeror. This power is often abused by drafting the form contract one-sidedly: unduly favourable to the offeror and with scant regard for the interests of the offeree. And as standard form contracts are seldom intended to be closely studied, the offeree frequently submits to terms of which he was unaware or which he did not understand and which, if invoked, would substantially change the value of his bargain or the balance of the remedies which are ordinarily available to and against him. In some cases a party may have to submit to unfair terms even if he is aware of them, because there is no other party who can satisfy his needs or who offers substantially different terms.

Secondly, the classical model of contract was both a response to and a reflection of a change in the social and economic role of contract at the time. Since then liberal individualism, the philosophy responsible for raising consensus from being merely the basis of contractual liability to being the touchstone of the entire contract, has been

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K.N. Llewellyn, What Price Contract? - An Essay in Perspective (1931) 40 Yale L.J. 704; F. Kessler, Contracts of Adhesion - Some thoughts about Freedom of Contract (1943) 43 Col.L.Rev. 629; N.S. Wilson, Freedom of Contract and Adhesion Contracts (1965) 14 I.C.L.Q.172; H.B. Sales, Standard Form Contracts (1953) 16 Mod.L.Rev.318.

largely superseded by a philosophy of greater socialization.

In spite of these fundamental changes in the substance and function of contract the principle of freedom of contract, in particular with regard to the constraints which it places on the power of the courts to control substantive unfairness, has remained in the position of "constitutional monarch"[1] right up to the present day. It has provided the framework within which almost all discussion of contractual fairness has taken place.

It is my belief that the principle that the courts do not concern themselves with the substantive fairness of a contract is contradicted or, at least, substantially qualified, by the actual practice of the courts, and that over the last three centuries discretionary powers of control have been assumed by the courts in various areas in order to give relief from unfair transactions.[2] The clearest instance in early law of a doctrine against unfair contracts was provided by the usury laws. Although the common law courts, which administered these laws, showed no inclination to extend their application, the Chancery courts, drawing on the policies underlying the usury laws,developed various doctrines to redress hard bargains in the seventeenth and eighteenth centuries. These were frequently applied until late in the nineteenth century and then, largely as a result of the fusion of law and equity, fell into

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1 The phrase is that of M.P. Ellinghaus, In Defense of Unconscionability (1969) 78 Yale L.J. 757, 775.

2 See, also, the survey by S.M. Waddams, Unconscionability in Contracts (1976) 39 Mod.L.Rev. 369.

disuse. Scots law with its single system of law and equity exercised a similar jurisdiction of discretionary justice primarily through the utilisation of a wide notion of fraud. This concept, as well as Chancery's protective doctrines, were whittled down during the nineteenth century, but in some forms continue to exist today. Since the nineteenth century contractual unfairness has arisen primarily where standard form contracts are used between parties with unequal economic power and resources. It would be wrong to suppose that the courts merely turned a blind eye to unfairness in those cases: while professing allegiance to freedom of contract they have attempted to limit the validity and effect of unfair terms by a variety of surreptitious and indirect techniques. Although these controls seldom involve a clear articulation that the contract or contract terms are too unfair to be given effect to there can be little doubt that, if the decisions are scrutinised as Lord Diplock has suggested,[1] by looking at what they say in the light of what they do, the courts have, in effect, been doing just that.

By the middle of the present century there was a growing realization in both legal systems that "covert tools are never reliable tools"[2] and that the indirect control of transactional unfairness was itself leading to uncertainty, was,in the absence of clear criteria, resulting in the striking down of fair contracts and also, that it was unable to deal comprehensively and effectively with the problem of

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1 A. Schroeder Music Publishing Co.Ltd. v. Macaulay /1974/ 1 W.L.R. 1308, 1315.

2 K.N. Llewellyn, Book Review (1939) 52 Harv.L.Rev. 700, 703.

unfair contracts.

As a result some courts assumed a more direct control of unfair contracts. This lead was neither widely followed nor universally welcomed and the legislature was moved to intervene. Following the lead of American law[1] the courts were recently given the statutory power to police contracts for unfairness in certain clearly circumscribed circumstances. However, the legislative provisions cover only limited areas and there is no consensus as to the extent to which courts may control unfair contracts falling outside the scope of these statutes nor is there any general agreement about the basis on which control - whether judicially assumed or conferred by statute - should proceed.

This work examines the various methods by which the courts have controlled contractual unfairness. This is done in order to determine not only the extent to which the unfairness of a contract is a factor which induces the court to exercise control, but also the policy grounds on which the courts proceed, the factors which render a contract objectionable, and the circumstances on which the granting of relief depends in each area.

Definition and Scope

The term "unfair" has no meaning in itself. Its content depends upon judicial interpretation and may differ according to the context in which it is used. As used here the term denotes unfairness in the contract itself - either through a specific term or through its overall effect. This use contrasts with the classical notion of an unfair

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[1] Uniform Commercial Code, section 2-302.

contract as one which has been imperfectly assented to, but corresponds to the meaning which is usually assigned to terms such as "unconscionable" or "unreasonable"[1] in the sphere of judicial control. Where these latter terms are habitually employed in specific types or areas of control they will generally be used in those contexts.

The question when a contract or contract term will be unfair is dependent on the test employed by the courts. In some cases a contract is regarded as unfair merely by reference to the substantive features of the contract. Mostly, however, the question of unfairness is also inextricably bound up with procedural aspects.[2] This entails that substantive features which may be perfectly fair in some circumstances will be regarded as unfair and constitute a sufficient ground for relief in other circumstances.

It is one of the legacies of freedom of contract that few of the methods of control focus directly on the substantive fairness of a contract. Many are formally concerned only with the propriety of contract formation. Some of these are discussed, but others such as misrepresentation, mistake and error have been omitted. Although the effect of the latter doctrines is often to relieve a party from a substantively unfair

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1 Yates, Exclusion Clauses in Contracts, 188-191 draws a conceptual distinction between "unconscionability" and "reasonableness". In my view neither of these terms has yet developed into distinct term of art and such a distinction is therefore unjustified.

2 The term "procedural" unconscionability was first used by A.A. Leff in Unconscionability and the Code - The Emperor's New Clause (1967) 115 U.Penn.L.Rev. 485 - a discussion about Section 2-302 of the Uniform Commercial Code - to denote unfairness in the process of contracting as opposed to substantive unfairness. It has since gained some currency on this side of the Atlantic.

contract they raise so many unconnected issues that it was thought inappropriate to include them in a work of this nature.

Method

Neither Scots nor English law has dealt with unfair contracts in a single uniform manner. Different types of unfairness and different factual settings have evoked different and often distinct types of control. In order to appreciate the full extent of control it is thus necessary to cover wide, and often disparate areas of contract law, which in turn makes strict classification difficult.

The work is divided into three parts. Part I which deals with the judicially developed remedies is subdivided into three sections: Section A examines mainly English law, but where there is substantial similarity between the systems, Scots law is discussed alongside it. Section B deals only with Scots law and Section C, which deals primarily, but not solely with the techniques used to combat unfair standard form contracts, covers both Scots and English law. Part II discusses the statutory tests of fairness and Part III examines critically the development of the judicial controls as they appear from the foregoing survey.

PART I

A - ENGLISH LAW

1 - USURY[1]

The prohibition of usury was the first large-scale attempt to control unfair contracts. In spite of the fact that formally the prohibition applied to a comparatively small number of the total contracts concluded the term usury soon came to encompass almost all extortionate bargains. The usury laws were of fundamental importance to the development of the various doctrines against unfair contracts, not only because they highlighted one particular manifestation of unfairness - unequal exchange of values or inadequacy of consideration, as it later became known - but also because they provided a conceptual framework which was to prove of the utmost importance to the way in which the judicial regulation of unfair contracts was later to proceed. It was natural that the influence of the usury laws was most strongly felt where financing arrangements were involved, but the insights gained there were rapidly given wider effect by the Chancery courts.

Usury has been defined as a stipulation in a contract of loan in terms of which the lender receives an additional amount as profit for the use of the money, and for the risk of its total or partial loss.[2]

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[1] See, generally, Ashley, English Economic History and Theory; 15 Encyclopaedia of Social Sciences,"Usury", 193-197; Bellot, The Legal Principles and Practice of Bargains with Moneylenders; Holdsworth, A History of English Law, especially Vol.VIII,100-113.

[2] Bellot, op. cit., 1.

Today this remuneration is generally called "interest" with the term "usury" reserved for such interest as may be excessive.

The medieval prohibition of usury found one of its sources in the Aristotelian notion that money, unlike plants and animals, does not reproduce itself - pecunia pecuniam parere non potest. From this it followed that the just price for a loan was the repayment of the principal sum without more. The prohibition was at the same time a reflection of Christian ethics: through it the moral injunction that a person should not take payment for helping his fellow-man was transformed into a rule of positive law. The underlying moral imperative was further strengthened by the economic reality of the time. The system of trade was primitive and provided little scope for productive capital investment with the result that where loans of money did occur it was predominantly for the purpose of "consumptive expenditure"[1] that is, for immediate use by the borrower during a period of crisis precipitated by some personal disaster such as illness or failure of crops. As the borrowers were generally either necessitous or extravagant "/t/he exaction of interest as payment for aid extended under such conditions could readily be described as a breach of Christian duty and a deliberate exploitation of another's need".[2] The circumstances in which loans occurred and the dire position of the people to whom they were given played a significant role in providing a moral basis for the prohibition of usury.

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1 Ashley, op. cit., Vol. 1, Part II, 435.

2 J.P. Dawson, Economic Duress and the Fair Exchange in French and German law II (1937) 12. Tul. L. Rev. 42, 44.

Although the laws of Scotland[1] and England in theory prohibited the taking of interest until well into the sixteenth century a considerable discrepancy had by that time developed between the ideal and the reality. Not only were certain groups such as the Jews exempted from the prohibition, but various commercial contracts and instruments were devised to circumvent the strict rule against usury.[2] The basis of these lay in the much earlier linkage of the principle of usury with the canonist doctrine of iustum pretium, which laid down that profit in buying and selling was acceptable only in so far as it provided a reasonable compensation for labour and risk.[3] Together these concepts formed part of an extensive and intricate philosophical system developed by the canonists which profoundly influenced not only the economic theories then prevailing, but also many aspects of private law.[4]

As early as the thirteenth century a distinction was drawn between a mere payment for the use of money and sums paid in order to compensate the lender for loss resulting from non-payment, either in the form of damnum emergens or lucrum cessans. Initially, the loan itself was gratuitous and additional payment was made only where the loan was not repaid on the stipulated date and where the loss was proved. By the end of the medieval period, however, this loss came to be presumed and the principle of the gratuitous loan became a fiction.[5]

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1 See, generally, Bell's Commentaries, 327-330.

2 See Bellot, op. cit., 32-37; Holdsworth, op. cit., 104-106.

3 See, Hahlo and Kahn, The South African Legal System and its Background, 460-461, and Ashley, op. cit., Vol. I, Part I, 146.

4 Dawson, op. cit., 44-45.

5 Holdsworth, op. cit., 103.

The growth in trade and the development of an economic system based on money led to a transformation in the views of the church and eventually a change in the official attitude became inevitable. In both Scotland and England legislation permitting the taking of interest was introduced.[1] Although this was an important development it was a reform rather than a revolution. Despite the fact that the taking of interest was thenceforth allowed it was only legal if it did not exceed a prescribed maximum rate. The principle of usury was thus not denounced. This, Ashley suggests, was due to the authority of the church which,

> caring for the masses of the people, for the weak and stupid, might think it well to maintain a prohibition which imposed no restriction on the activity of the traders in the towns, who were well enough off to take care of themselves. The original prohibition had really aimed at preventing the oppression of the weak by the economically strong. The gradual exemption from the prohibitions of methods of employing money which did not involve oppression, instead of obscuring the original principle, may be said to have brought it out more clearly.[2]

During the next few centuries variations in the permitted maximum rate of interest occurred, but otherwise the usury statutes underwent no major changes.

Under the concerted onslaught of liberal individualism and the laissez-faire economists the attitude to usury, as to many other aspects of commercial law, underwent a profound change in the nineteenth century.[3] Rather than attack the taking of usurious interest,

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1 In respect of Scotland see the Acts of 1597, c. 247 and 1621, c.28. For English law, see Holdsworth, op. cit.

2 Ashley, op. cit., Vol. I, Part II, 438-439.

3 See, 15 Encyc. Soc. Sci., op. cit., 196-197.

it became the conventional wisdom to defend it. The repeal of all usury laws in 1854 therefore came as no surprise.[1]

Although those laws which permitted the taking, but controlled the rate of interest constituted a departure from earlier notions of commutative justice and were indicative of greater commercial freedom, they also retained sufficient protective measures to show that the earlier postulates had not been entirely jettisoned. The condemnation of excessive profits implicit in them gained an influence much wider than the immediate field in which these laws operated. The standards of equivalence demanded by the usury laws familiarised the Chancery courts with the notion of fair exchange in contracts generally[2] and provided them with a conceptual framework which facilitated intervention on similar grounds in areas falling outside the immediate scope of the laws of usury, such as catching bargains with heirs, unconscionable bargains with those suffering from weakness and necessity and forfeitures generally. In retrospect the movement of ideas from the area of usurious loans to that of unfair transactions in equity was natural and not overly tortuous. The fundamental aim of the usury laws, namely the protection of weak, defenceless borrowers from often rapacious moneylenders was, after all, equally apposite in the dramatic situation of the cases which confronted equity.

The repeal of the usury laws left the borrower unprotected and the moneylender free to pursue his business without fetters. Although

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1 17, 18 Victoria c.90.

2 See, J.P. Dawson, Economic Duress - An Essay in Perspective (1947) 45 Mich. L. Rev. 253, 278.

the Chancery courts endeavoured to intervene on behalf of the borrower where their jurisdiction allowed, such protection was of course limited. Scots law which operated without a separate equity jurisdiction and was consequently even more thoroughly affected by freedom of contract, provided even less protection to borrowers than English law. The legislature, moved largely as a result of the ensuing exploitation of borrowers by the moneylenders, put the Moneylender Act 1900 on the statute book. This Act and the Moneylender Act 1927 came into force in both Scotland and England. These Acts, as well as their successor, the Consumer Credit Act 1974 are examined in Part II.

2 - INADEQUACY OF CONSIDERATION IN THE COMMON LAW

The enforcement of the usury statutes was the responsibility of the common law courts. But despite their experience in this area they were unwilling to use the usury jurisdiction as a basis for extending, by analogy, that power of control to other contracts which stipulated for an unequal exchange. English law never recognised the civil law doctrine of laesio enormis and the common law courts took a dismissive attitude towards the question of the adequacy of consideration. The general rule, it was said, is that the courts will not inquire into the adequacy of consideration.[1] The position today remains unchanged. To a large extent the refusal to review the adequacy of consideration is connected to the origin and function of the doctrine of consideration: it arose as a technical formula for delimiting those promises to which legal liability should attach and it was never intended as an instrument for attacking unequal agreements. It is thus understandable that "/i/n the common law system the struggle over consideration was a struggle to express the results of procedural developments in areas where policy and fairness required enforcement, not cancellation or revision."[2]

The principle that consideration need not be adequate has not precluded the courts from using the doctrine as a device to combat unfairly procured contracts under the pretext that there was a complete absence of consideration. This technique is frequently used

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1 See, for example, Basset v. Nosworthy (1673) Rep.t.F.102,104. Also Chitty on Contracts SS 143-146; Treitel, Law of Contract, 56-57 who does however recognise that the rule is subject to a number of exceptions.

2 J.P. Dawson, Economic Duress - An Essay in Perspective (1947) 45 Mich.L.Rev. 253,277.

to deny validity to an agreement concluded under pressure from a promisee who threatens a breach of an already existing contractual duty and whose only consideration in return for the new promise is to perform his pre-existing duty.[1] A similar situation is presented by those cases where a debtor[2] or creditor[3] has, under pressure from his counterparty, compromised a claim and accepted in full settlement an amount less than that which is in fact owed. Again the courts have determined that a promise to pay only part of what is owed will not provide consideration for the accord. It has been correctly pointed out that if the purpose of this technique is to refuse validity to agreements induced by improper pressure the formula used is inappropriate. By not focussing on the general merits of each agreement the courts are forced to strike down not only those agreements which are improperly obtained and unfair but also those which are not obtained by any unfair dealing and which are entirely reasonable and fair.[4]

Despite the fact that technically consideration need not be adequate a few early cases exist in which common law courts gave

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1 Stilk v. Myrick (1809) 2 Camp.317. According to the earlier case of Harris v. Watson (1791) Peake 102, the agreement was invalid because it was against public policy. Since Stilk v. Myrick it has been customary to base the invalidity on the absence of consideration. See also The Atlantic Baron /1978/3 All E.R.1170; Pao On v. Lau Yin /1979/3 All E.R.65, 76-78. Also J. Adams, Note (1979)42 Mod.L.Rev.557.

2 Foakes v. Beer (1884)9 App.Cas.605, approving the rule in Pinnel's case (1602)5 Co.Rep.117a.

3 D.& C.Builders Ltd. v. Rees /1966/2 Q.B.617, discussed by W.R. Cornish (1966) 39 Mod.L.Rev.428.

4 R.J. Sutton, Duress by Threatened Breach of Contract (1974)20 McG. L.J. 554-555; S.M. Waddams, Unconscionability in Contracts (1976)39 Mod.L.Rev.369, 388; Treitel, op. cit., 73-74, 89.

relief from agreements, ostensibly on the sole ground that they involved a grossly unequal exchange of values. On the whole these cases are of a very early date, the reports are brief and the principles underlying the decisions are uncertain and ambiguous.

In the earliest case, James v. Morgan[1], the defendant contracted to buy a horse from the plaintiff. The purchase price was to be a barley-corn for the first nail in the horse's shoe, two for the second and so on, doubling the amount for each nail. As the horse's hooves contained thirty-two nails he was obliged to pay five hundred quarters of barley-corn, the value of which far exceeded that of the horse. In assumpsit by the plaintiff the defendant pleaded that he should be directed to pay in damages only the value of the horse which was £8. The court complied "for a catching bargain shall not be taken advantage of".[2]

In both Earl of Chesterfield v. Janssen[3] and Hume v. United States of America[4] the judges were of the opinion that the principle of James v. Morgan was strengthened by Thornborow v. Whitacre.[5] In that case plaintiff paid defendant 2s.6d. and agreed to pay a further £4.17s.6d on the completion of defendant's performance. Defendant in turn undertook to deliver to plaintiff two grains of corn on Monday 29 March and four grains a fortnight later and so on, doubling the amount for each fortnight for a year.[6] Defendant's

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1 (1664) 1 Lev. 111.

2 6 Mod. 305 n. per Hyde C.J.

3 (1750) 2 Ves. 125.

4 (1889) 132 U.S. 406.

5 (1704)2 Ld.Ray.1164; also reported as Thornborough v. Whitacre (1703) 6 Mod.305.

6 The Ld. Ray report refers to "every other Monday" which was interpreted by Holt C.J. as alternate Mondays. The Modern Report, however, speaks of "every Monday during the year".

counsel argued that because of his client's poverty performance was impossible and that he was thus not liable on the agreement. The case was eventually settled out of court when it became clear that the court would award only "reasonable"[1] damages to the plaintiff.

In Earl of Chesterfield v. Janssen, Lord Hardwicke L.C., in setting out the different types of fraud which may affect the validity of an agreement, referred to fraud which "may be apparent from the intrinsic nature and subject of the bargain itself; such as no man in his senses and not under delusion would make on the one hand, and as no honest and fair man would accept on the other; which are unequitable and unconscientious bargains" and cited James v. Morgan in support.[2] In terms of his Lordship's analysis that type of fraud is inferred solely from the gross inadequacy of the consideration or the gross inequality in the values of the respective prestations and it exists quite separately from the types of fraud which might affect bargains with expectant heirs or bargains between parties with unequal bargaining power.

It may be argued that the inadequacy of the reports of James v. Morgan and Thornborow v. Whitacre makes them doubtful authority for a separate head of fraud and that, at most, they are applications of the principles which govern the measure of damages. Yet in the much later case of Hume v. United States of America, Fuller C.J. referred to and approved both these cases. The plaintiff had undertaken to supply certain goods to a government hospital. In terms of the written contract the price was 60c per pound, whereas the

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1 (1703)6 Med. 305.

2 (1750)2 Ves. 125.155.

current market value was less than 2 c per pound. As the purchase price had remained unpaid the plaintiff claimed the price as set out in the document. The defendant pleaded that it had intended to buy at 60c per hundredweight and that the price stipulated in the document was due to a clerical error. Fuller C.J., in giving judgment for the defendant, accepted Lord Hardwicke L.C.'s view that a contract which is inequitable and unconscientious on its face may be relieved from on the ground of fraud and he interpreted James v. Morgan and Thornborow v. Whitacre as authorities for a doctrine which empowers the courts to reduce an extortionate and unconscionable price according to the fair entitlements of the parties.[1]

The judgment did not, however, rest solely on that ground. The particular facts of the case also raised issues of public policy and the Chief Justice maintained that parties must realize that the public officers with whom they deal are agents of the government and as such must act bona fide and fair.[2]

The cases just referred to are but scant authority for the view that a common law doctrine existed in terms of which relief would be given from an agreement solely because of inadequate consideration. Earl of Chesterfield v. Janssen and Hume v. United States of America show that in later times the review as to the adequacy of consideration was subsumed under the ground of equitable fraud. This phenomenon will be discussed later.

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1 (1889) 132 U.S. 406.

2 Ibid.

3 - INADEQUACY OF CONSIDERATION IN THE COURT OF CHANCERY

A number of late sixteenth century and early seventeenth century cases create the impression that the Chancery courts were prepared to set aside agreements on the ground of inadequacy per se. The reports are, however, so brief that it is impossible to state with certainty the ground on which the courts based their decisions. In Oddy v. Torlese[1] the plaintiff had undertaken to pay £950 to the defendant. He proceeded to pay £500 and both parties then agreed that until such time as the plaintiff could pay the remaining £450 in a lump sum he should pay the defendant £80 annually. It appeared that the plaintiff had on that account already paid £300 more than the outstanding £450 plus interest. The court held that the plaintiff need make no further payments but that he could not reclaim the amount by which the £450 owed had been exceeded. No reason was given in support of the judgment. The court in Fawcet v. Bowers[2] similarly gave no reason for setting aside a contract in terms of which the plaintiff in return for £800 had granted the defendant an annuity of £60 for seven years. Maskeen v. Cole[3] concerned the sale for £50 of a legacy valued by the court at £166. The Lord Chancellor declared that "under this consideration I should have made no difficulty in relieving the plaintiff, as not having received one-half of his legacy." The court was, however, precluded from following this course because "with his eyes open [the plaintiff] agrees to

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1 (1685) 1 Ver. 352.

2 (1693)2 Ver. 287. See also Plumbe v. Carter (1775)1 Cowp. 116 and Jestons v. Brooke (1778)2 Cowp. 793 where Lord Mansfield refused an action for money had and received on the ground that the sum claimed was, although not usurious, hard and unconscionable.

3 (1733)2 Madd. 421n.

this contract he has made ... and confirms it by a new deed."

In contrast to these by no means unequivocal authorities are those cases wherein it is specifically denied that inadequacy of consideration per se is a ground for setting aside a transaction. The report of Wood v. Fenwick serves as a good example:

> The plaintiff Wood's wife, as heir to her brother, had an inn in Newcastle descended to her, which was let at £69 per ann., but was subject to a mortgage. The plaintiffs, being poor, were inveigled to sell this inn, and all their interest therein, to the defendant Fenwick for £80, and after brought a bill for relief against the mortgage, and all his other debts; and at the end of the bill pray relief on the whole matter, and the administrator was made defendant. On hearing of the cause, my Lord Keeper was of opinion, that though the purchase was not a fair bargain, yet no such fraud appeared as to set it aside.[1]

And in Stephens v. Bateman, Lord Thurlow L.C. said that "It was manifest it was a hard bargain ... But is that a ground to set aside the conveyance? - No. - The cases are express that the court will not set aside the conveyance on that ground only."[2]

In view of these strong and direct denials that inadequacy of consideration was ever in itself a sufficient ground for setting aside an agreement in equity it is better to regard the few cases which imply the contrary as wrong.

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1 (1702) Pr.Ch.206.

2 (1778)1 Bro.C.C. 22, 26.

4 - EQUITY'S DOCTRINES AGAINST UNFAIR CONTRACTS

It would be wrong to deduce from the formal refusal by both the common law and the Chancery courts to set aside transactions solely by reason of the inadequacy of consideration that a judicial blind eye was always turned to an unequal exchange between the parties or to unfairness in contracts generally. Although direct common law intervention in unfair contracts was, apart from the doubtful precedents referred to above, limited, it was equity which, especially from the latter part of the seventeenth century, carried on the spirit of the usury laws by developing elaborate structures for the control of unfair contracts.

This came mainly through three separate doctrines: the doctrine against forfeitures and penalties, the principle of withholding specific performance where a contract is unfair, and the doctrine against equitable fraud. The doctrine against penalties and forfeitures was aimed at specific clauses and therefore had a limited field of operation. The principle of specific performance on the ground of unfairness applied to all contracts, but the control was limited, because as we shall see, it still left the plaintiff/creditor free to claim damages at law. Of the three doctrines against unfairness it was equitable fraud which gained the widest application.

(a) Equity's doctrine against forfeitures

The present-day law in respect of the equity of redemption, forfeiture of leases for non-performance of contractual terms and penal clauses, find a common origin in the jurisdiction of the Court of Chancery against forfeitures in general.[1] Bonds, mortgages and

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[1] See, generally, Yale, Lord Nottingham's Chancery Cases II, Selden Society, Vol. 79, 7-62.

leases were the main areas in which equity exercised a policy of relief against forfeitures. Originally the basis of this relief was similar in all three cases, but eventually rules peculiar to each of these factual settings developed.[1] The law governing the forfeiture of money paid is the product of later developments but it has been, because of the close resemblance in nature and effect between penal clauses and forfeiture of money paid, subject to the same considerations as those that influenced the development of the law relating to other forfeitures.

The equitable jurisdiction against forfeitures is the earliest example of the courts' refusal to give effect to clear and unambiguous terms in contracts by reason of their unfairness. Although the law in respect of forfeitures has, in many instances, crystallised into technical doctrines far removed from the original spirit of equity, it still shows signs of the considerations that initially compelled judicial intervention. As such it is an important exception to the generally accepted view that the fairness of exchange is legally irrelevant.

(i) Forfeiture of mortgages: the equity of redemption[2]

The equity of redemption, an equitable estate arising in the mortgagor and carrying with it the power to redeem the mortgaged

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1 A.W.B. Simpson, The Penal Bond with Conditional Defeasance (1966) 82 L.Q.R.392, 416.

2 See, A.W.B. Simpson, op. cit.; Turner, The Equity of Redemption, especially 17-42 and 175-183; Hanbury, Modern Equity, 340-346; Keeton and Sheridan, Equity 166-178 and 202-209.

property notwithstanding the fact that the contractual date for redemption has passed, developed in the Courts of Chancery during the late-sixteenth and the seventeenth centuries. It was conceived as a remedy to the harshness of the common law which required strict performance of the mortgage agreement with the result that the mortgagor who failed to repay the mortgage money on the appointed day lost his legal right of redemption for ever. The Chancellor refused to countenance the forfeiture of the mortgaged property and enforced reconveyance of it to the mortgagor where the latter tendered the full amount within a reasonable time after the forfeiture. Initially the Chancery courts assumed jurisdiction on the ground of conscience[1], regarding it as unfair that the mortgagee should keep the mortgaged property absolutely when the amount secured by the mortgage may be substantially less than the value of the property.[2] The unfairness of a successful reliance on the forfeiture clause of course lay in the gross disparity between the values exchanged which would result from it. Later, relief was also made dependent upon a showing of special circumstances of hardship or fraud which tainted the agreement. However, by the middle of the seventeenth century the equity had become an established incident of mortgages and the Chancellors ordered reconveyance of the mortgaged property as a matter of course, where the mortgagor tendered the capital together with a reasonable sum for the use of the money,[3] "a practice that

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1 Turner op. cit., 23.

2 G.L. Williams, The Doctrine of Repugnancy III: 'Clogging the Equity' and Miscellaneous Applications (1944)60 L.Q.R. 190.

3 Turner, op. cit., 13.

derived from the wide and undifferentiated jurisdiction of earlier times to relieve against the unconscionable use of legal rights generally."[1]

This extension and consolidation of the Chancellors' jurisdiction coincided with a perfunctory transformation in the basis of judicial intervention. In accordance with its rule of looking at the intent rather than the form of transactions, equity came to regard mortgages and likewise penal bonds, as essentially devices aimed at securing loans so that when the debtor had paid the creditor the principal sum, interest and cost, it was all that the latter could, in fairness, expect for the use of his money. "Equity suffers not Advantage to be taken of a Penalty or forfeiture where Compensation can be made."[2] In essence this meant that the courts would not allow a forfeiture where it would lead to a gross disparity in the values exchanged and where the creditor could be suitably compensated for his loss. No doubt the lingering dislike of usury played an important underlying role in this development.[3] This "principle of compensation" came to govern the validity of forfeitures not only in respect of mortgages, but also in relation to leases and penal bonds. It is clear, however, that the change in rationale was less significant than appears at first sight. Although intervention was then activated by a general disapproval of security

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1 Yale, op. cit., 13.

2 R. Francis, Maxims of Equity, as cited by Yale, op. cit., 16.

3 See G. & C. Kreglinger v. New Patagonia Meat and Cold Storage Co. Ltd. [1914] A.C.25, 54 per Lord Parker.

devices, the fundamental reason for the court's action remained the inequality of the exchange which might result from a forfeiture. What had happened was that the general standard on which intervention was initially based had developed into a more particularised and rigid legal rule.

The relief given to mortgagors was of course a direct interference with the express agreement of the parties and early in the development of the jurisdiction the courts had to deal with attempts to circumvent the jurisdiction. These took many different forms, for example, stipulating that the right to redeem was limited to the mortgagor personally[1] or that the money could not be repaid until some future date[2], options given to a mortgagee to buy the equity of redemption[3] or stipulations for collateral advantage.[4] These the courts steadfastly refused to allow and the principle was soon established that any terms in a mortgage agreement which limited or hampered the power of redemption was void. The vehemence with which the courts protected their creation from infringement stemmed from two considerations. Firstly, the Chancellors regarded the equity of redemption as an inalienable incident of mortgages, and secondly the mortgagor, during the period of development of the equity of redemption had usually been an impoverished landowner with little

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1 See, for example, Howard v. Harris (1683) 1Vern. 190.

2 Talbot v. Braddill (1683) 1 Vern. 183; affirmed by Jeffreys L.C. in (1686) 1 Vern. 394. Knightsbridge Estates Trust Ltd. v. Byrne [1939] Ch.441.

3 Jennings v. Ward (1705) 2 Vern. 520.

4 G. & C. Kreglinger v. New Patagonia Meat and Cold Storage Co.Ltd. [1904] A.C.25. The case really involved a floating charge redeemable on one month's notice, but the House of Lords was of the opinion that the law of mortgages was applicable.

bargaining power and thus in great need of protection from the money-lenders of the day. As Lord Northington L.C. expressed it in Vernon v. Bethell

> ... /T/here is great reason and justice in this rule /that the mortgage agreement may not contain an option for the sale of the equity of redemption/, for necessitous men are not, truly speaking, free men, but to answer a present exigency, will submit to any terms that the crafty may impose upon them.[1]

Under these circumstances the Court of Chancery was not prepared merely to sit back and observe weak and oppressed mortgagors bargain away the protection given by the equity of redemption.

The rules against the fettering of the equity of redemption were enforced without reference to the fairness of the transaction.[2] This rigidity necessarily led to injustice in that perfectly fair bargains were struck down.[3] Lately this approach has met with some opposition from the courts. As Lord Haldane, L.C. said in Kreglinger v. New Patagonia Meat and Cold Storage Co. Ltd.:

> It was, in ordinary cases, only where there was conduct which the Court of Chancery regarded as unconscientious that it interfered with freedom of contract. The lending of money, on mortgage or otherwise, was looked on with suspicion, and the Court was on the alert to discover want of conscience in the terms imposed by lenders... /I/t is inconsistent with the objects for which they were established that these rules should crystallize into technical language so rigid that the letter can defeat the underlying spirit and purpose.[4]

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1 (1762)2 Eden 110,113.

2 The rules had in fact become so fossilised that Plowman J. could say in Lewis v. Frank Love Ltd. /1961/ 1 W.L.R.261, 270 that "... the doctrine of clog on the equity is a technical doctrine which is not affected by the question whether in fact there has been oppression..."

3 See, for example, Samuel v. Jarrah Timber and Wood Paving Corp. Ltd. /1904/ A.C. 323, 325 per Earl of Halsbury L.C.

4 /1914/ A.C. 25, 36 and 37-38.

This view, together with the realisation that the present-day mortgagor is in many cases a vastly different species from his oppressed and necessitous predecessor have led to the rejection of the rigid rules which developed through the centuries and a reassertion of the original bases of intervention. As Lord Parker said in the same case:

> /T/he defendants in this case are appealing to the equitable jurisdiction of the Court for relief from a contract which they admit to be fair and reasonable and of which they have already enjoyed the full advantage... In every case in which a stipulation by a mortgagee for a collateral advantage has, since the repeal of the usury laws, been held invalid, the stipulation has been open to objection either (1) because it was unconscionable, or (2) because it was in the nature of a penal clause clogging the equity arising on failure to exercise a contractual right to redeem,or (3) because it was in the nature of a condition repugnant as well to the contractual as to the equitable right.[1]

These statements were extensively discussed by Lord Greene M.R. in Knightsbridge Estates Trust, Ltd. v. Byrne.[2] The case concerned the mortgage of a large freehold estate for £310,000, which was to be repaid by instalments over forty years. The mortgagors wished to redeem after only five years and the matter was brought before the court. The Master of the Rolls, in the course of a judgment in which he held the delay in the redemption date to be valid, corrected "the impression, which was gathering momentum before the decision, that the court /could/ cancel such a stipulation on the ground that the length of the period is unreasonable,"[3] with reference only to the terms of the mortgage agreement. Equity, his

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1 Ibid., 46, 56.

2 /1939/1 Ch. 441.

3 Hanbury, op. cit., 342.

Lordship maintained, will not give relief from the contractual terms in a mortgage transaction merely because they are unreasonable, but only if they are oppressive and unconscionable and in order to determine whether that is the case the mortgage must be scrutinised in its proper business setting.[1]

> In the circumstances it was the most natural thing in the world that the respondents should address themselves to a body desirous of obtaining a long term investment for its money. The resulting agreement was a commercial agreement between two important corporations experienced in such matters, and has none of the features of an oppressive bargain where the borrower is at the mercy of an unscrupulous lender... /W/e are not prepared to view the agreement made as anything but a proper business transaction.[2]

But in Cityland and Property (Holdings) Ltd v. Dabrah,[3] Goff J. refused to give effect to a term in a mortgage agreement which stipulated for payment of a collateral advantage on the basis that it was "unfair and unconscionable" or "unreasonable" in the circumstances.

The whole question of the circumstances under which a clog on the equity of redemption will be held invalid was reviewed by Browne-Wilkinson J. in the recent case of Multiservice Bookbinding Ltd. v. Marden.[4] The plaintiff company, needing £36,000 to buy new business premises, approached the defendant who agreed to advance the sum. A mortgage was executed in 1967 charging the building which plaintiffs were to buy with the money, as security for the loan. Apart from stipulations as to the payment of interest the mortgage agreement

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1 /1939/ Ch.441, 455.

2 Ibid.

3 /1968/ Ch. 166.

4 /1979/ Ch. 84.

prescribed inter alia that the loan could neither be called in or redeemed during the first ten years and, by clause 6, that any sum payable as principal or interest was to be "increased or decreased proportionately, if at the close of business on the day preceding the day on which payment is made the rate of exchange between the Swiss franc and the pound sterling shall vary by more than three per cent from the rate of 12.07$\frac{5}{8}$ francs to £1", the rate prevailing at the date of the mortgage.

As the pound sterling dropped dramatically in value vis-à-vis the Swiss franc during the ten years from 1967, the interest which the plaintiff company was obliged to pay was substantially larger than it would have been without the index-linking provision of clause 6 and the plaintiffs brought a summons to determine whether the terms of the mortgage were not unenforceable in that they stipulated for an unreasonable collateral advantage.

Browne-Wilkinson J. made an extensive review of the cases referred to above and came to the conclusion that "/S/ince the repeal of the usury laws there has been no general principle that collateral advantages in mortgages have to be 'reasonable'"[1] Just as Lord Greene M.R. did in the Knightsbridge Estates Trust case, he distinguished between a test of reasonableness and one of unconscionableness, and declared:

> /T/o be freed from the necessity to comply with all the terms of the mortgage, the plaintiffs must show that the bargain, or some of its terms, was unfair and unconscionable: it is not enough to show that, in the eyes of the court, it was unreasonable. In my judgement a bargain cannot be unfair

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1 Ibid., 105.

> and unconscionable unless one of the parties to it has imposed the objectionable terms in a morally reprehensible manner, that is to say, in a way which affects his conscience.[1]

Although the approach of Browne-Wilkinson J. is to be broadly welcomed as a consolidation of the movement away from the rigidity which has characterised this aspect of the law relating to the equity of redemption for such a long time, the terminological distinction between "unreasonable" and "unconscionable" does seem unnecessarily arbitrary. The test of reasonableness has, after all, often been employed in a way which suggests that it refers to the fairness of an agreement in its totality. In his Lordship's opinion "unreasonableness" refers solely to the merits of the terms, whereas "unconscionability" also requires a showing that an "unfair advantage has been taken of the borrower"[2] or that the "bargain has been procured by unfair means."[3] The judge did, however, alleviate the evidential burden on the mortgagor when he said that if the agreement contains an "unusual or unreasonable stipulation the reason for which is not explained, it may well be that in the absence of any explanation, the court will assume that unfair advantage has been taken of the borrower."[4] Applying this reasoning to Cityland and Property (Holdings) Ltd. v. Dabrah[5] Browne-Wilkinson J. said that "/b/earing in mind the relative strength of lender

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1 Ibid., 110.

2 Ibid., 111.

3 Ibid., 110.

4 Ibid., 111.

5 /1968/ Ch. 166.

and borrower, the size of the premium and the lack of any explanation or justification for it, the premium ... was unconscionable and oppressive."[1]

Turning to the case in hand the judge said that the "Swiss franc uplift" clause was justified as a device by which the mortgagee could ensure that he is repaid the real value of his money. There was, in addition no great inequality of bargaining power between the parties, the borrowers were protected by independent solicitors and the lenders were not guilty of sharp practice.[2] In those circumstances the agreement could not be described as unconscionable.

This case indicates quite clearly that the courts will give relief to a mortgagor if the contract stipulates for the payment of a sum grossly in excess of the amount of the principal sum plus interest and if that stipulation can be explained by inequality in the bargaining strength between mortgagor and mortgagee. There has thus been a return to the considerations which originally activated equity's intervention.

(ii) Forfeiture of Leases

There is no doubt that courts of equity have from the earliest times exercised the right to relieve against clauses stipulating for the forfeiture of a lease upon breach of any of the terms of the lease contract.[3] This was merely another application of the

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1 /1979/ Ch.84, 110.

2 Ibid., 111.

3 Webber v. Smith (1689)2 Vern. 103; Nash v. Earl of Derby (1705) 2 Vern. 537; Cox v. Higford (1710)2 Vern. 664; Popham v. Bampfeild (1682)1 Vern. 79; Grimston v. Lord Bruce (1707) 1 Salk. 156; Davis v. West (1806)12 Ves. 475; Bargent v. Thomson (1864) 4 Giff. 473.

equitable jurisdiction against forfeitures generally.

The underlying principles on which relief is granted in this field are similar to those which governed the giving of relief in the related areas of penal bonds and mortgages. They are clearly expressed by Lord Erskine in the important case of Sanders v. Pope:

> There is no branch of the jurisdiction of this Court more delicate than that, which goes to restrain the exercise of a legal right. That jurisdiction rests only upon this principle; that one party is taking advantage of a forfeiture; and as a rigid exercise of the legal right would produce a hardship, a great loss and injury on the one hand arising from going to the full extent of the right, while on the other the party may have the full benefit of the contract, as originally framed, the Court will interfere; where a clear mode of compensation can be discovered. Of this nature is the case, that constantly occurs, confirmed by Statute... giving a more ready mode of relief at law: a contract to pay rent, with a covenant and clause of re-entry for breach. The obvious intention is to secure the payment of the rent; that the landlord may not be put to his action of debt, coming from time to time against an insolvent estate; but may be enabled to recover possession of the premises. In that case equity is in the constant course of relieving the tenant... and upon payment of the rent and all expenses will not permit the tenant to be turned out of possession; considering, that in the one case frequently great hardship might be the consequence; in the other, the party being placed in the same situation, there is in general no hardship.[1]

Courts of equity were also prepared to give relief against forfeiture on account of breaches other than payment of rent, such as obligations to repair or not to assign the lease where it was possible to give the lessor adequate compensation for the breach.[2] However,

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1 (1806)12 Ves. 282, 289. Similar principles are expressed in Chandless-Chandless v. Nicholson [1942]2 K.B. 321, 323; Belgravia Insurance Co.Ltd. v. Meah [1964]1 Q.B.436, 444-445; Barton Thompson & Co. Ltd. v. Stapling Machines Co.[1966]Ch.499,509 where Pennycuik J. suggests that this jurisdiction may be extended so as also to apply to leases of chattels; Richard Clarke & Co.Ltd. v. Widnall [1976] 1 W.L.R. 845; Athabasea Realty Co.Ltd. v. Lee [1976]67 D.L.R. (3rd) 272.

2 See Webber v. Smith (1689)2 Vern. 103; Cox v. Higford (1710)2 Vern. 664; Davis v. West (1806)12 Ves. 475; Sanders v. Pope (1806)12 282. Forfeitures for breach of a covenant to pay rent and for covenants to insure are now regulated by statute, but the law as expressed in many of these statutes is founded on the principles established in the old Chancery cases: Belgravia Insurance Co.Ltd. v. Meah [1964]1 Q.B.436, 444 per Lord Denning M.R.

in Wadman v. Calcraft[1] Lord Eldon L.C. held that relief was only possible where the forfeiture arose as a result of a breach of payment provisions and not where it is the result of the breach of some other covenant. The Lord Chancellor reiterated this opinion in Hill v. Barclay[2] despite the decision in Sanders v. Pope where Lord Erskine decided that relief was in the discretion of the court in a case where a forfeiture resulted from a breach of a covenant to do repairs, and the money, together with all costs as well as an increase because of the loss of time, was spent later and did not injure the landlord. It was Lord Eldon L.C.'s strict attitude to the enforcement of contractual obligations which was more acceptable in an era of laissez faire.[3] This approach created considerable hardship[4] and has now been overruled by the House of Lords in Shiloh Spinners Ltd. v. Harding[5] where Lord Wilberforce expressed the relevant principles as follows:

> /W/e should reaffirm the right of courts of equity in appropriate and limited cases to relieve against forfeiture for breach of covenant or condition where the primary object of the bargain is to secure a stated result which can effectively be attained when the matter comes before the court, and where the forfeiture provision is added by way of security for the production of that result. The word 'appropriate' involves consideration of the conduct of the applicant for relief, in particular whether his default was wilful, of the gravity of the breaches, and of the disparity between the value of the property of which forfeiture is claimed as compared with the damage caused by the breach.[6]

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1 (1804) 10 Ves. 67, 69.

2 (1811) 18 Ves. 56, 60.

3 See Bracebridge v. Buckley (1816)2 Price 200; Barrow v. Isaacs & Son /1891/1 Q.B.417.

4 Barrow v. Isaacs & Son /1891/ 1 Q.B. 417.

5 /1973/ A.C.691.

6 Ibid., 723-724.

And Lord Simon of Glaisdale commented that the strict application of freedom of contract in Hill v. Barclay[1] and subsequent cases

> seems to me to demonstrate an abnegation of equity, and to show that the trail from Hill v. Barclay leads into a juristic desert... The last hundred years have seen many examples of relaxation of the stance of regarding contractual rights and obligations as sacrosanct and exclusive of other considerations: though these examples do not compel equity to follow - certainly not to the extent of overturning established authorities - they do at least invite a more liberal and extensively based attitude on the part of courts which are not bound by those authorities. I would therefore myself hold that equity has an unlimited and unfettered jurisdiction to relieve against contractual forfeitures and penalties.[2]

As in the case of mortgages, the court will therefore relieve from a forfeiture if exercise of the right of forfeiture would lead to hardship on the one side and unfair advantage on the other, and where the landlord can be suitably compensated for his loss. In short, where a clause functions primarily as a security device the court will not allow reliance on it where it would lead to a gross imbalance in the respective performances of the parties.

(iii) Penal Clauses

Parties to a contract frequently covenant that in the event of a specified breach or breaches the party in default will pay a certain sum of money to the injured party. Such a provision not only serves as a form of security for the performance of the primary obligation, but it also obviates the problem of calculating damages

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1 (1811) 18 Ves. 56.

2 [1973] A.C. 691, 726.

after the breach where these may be uncertain or difficult to quantify. The courts often deny these clauses enforcement and by so doing they place a clear limitation on the principle of freedom of contract. The control exercised by the courts dates back to the era of canon law and was initially greatly influenced by the prohibition against usury. Although the grounds upon which modern courts in England and Scotland distinguish between enforceable and unenforceable damage clauses are similar, the development of control proceeded along different lines in the two jurisdictions.

Historical Survey: English Law.[1]

The penal bond upon a condition was the earliest form of contractual obligation. The purpose of the bond was to secure performance of the condition; where the condition was unperformed the penal sum could be claimed. The Chancery courts at a very early stage assumed jurisdiction against penal bonds. Although relief from a penal bond had been given as early as the fourteenth century[2] they survived the canonist era, because, paradoxically, they were regarded as compensatory and not usurious in nature.[3]

By the sixteenth and early seventeenth century such reasoning had become unacceptable and the need to mitigate the harshness of penal bonds was clearly felt. And although the basis of Chancery's

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1 See generally, A.W.B. Simpson, The Penal Bond with Conditional Defeasance (1966) 82 L.Q.R. 392; Yale, Lord Nottingham's Chancery Cases II, Selden Society, Vol.79, 7-30; Williston on Contracts Vol.5. Sections 769-811.

2 Yale, op. cit., 27 cites a case in the eyre of Kent in 1313-1314.

3 Simpson, op. cit., 412-413.

jurisdiction had not yet become settled, Holdsworth is of the opinion that intervention occurred because "it was obviously against conscience that a person should recover a sum of money wholly in excess of any loss incurred."[1]

By the time of the Restoration equity's jurisdiction against penal clauses and forfeitures generally had become crystallised. They were seen as security devices and were not allowed to stand where the creditor could be suitably compensated for his loss. Although there were already signs in the seventeenth century that the rules governing judicial intervention were growing more rigid, as for example in the striking down of clauses merely on the ground of being "security" without more, it was only later that the modern distinction between penalties and liquidate damage clauses,[2] based on whether the clause served merely to enforce fulfilment of a contractual obligation, or whether it was a genuine assessment of the damages that may possibly flow from a breach, became generally accepted.[3] After the development of assumpsit the penal bond was used far less frequently than before but the principles which were

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1 History of English Law, Vol. V, 393.

2 Simpson, op. cit., 420 suggests that because contracts had become more secure after the rise of assumpsit, the courts began to disapprove of security devices inserted in contracts. They regarded the means of securing the performance of obligations as their sole prerogative. This view also explains the subsequent distinction between penalties and liquidate damage clauses. The courts, in the words of Lord Justice Clerk Inglis in Craig v. M'beath (1863) IM.1020, 1022, simply regarded it as "not legal to stipulate for punishment."

3 See, for example, Sloman v. Walter (1788) 1 Bro. C.C. 418.

originally developed in respect of penal bonds were eventually extended to penal clauses in all contracts. Although this view of penal clauses was pioneered by the Chancery courts it was taken over by the common law when it eventually followed equity into this area.[1]

The assumption of jurisdiction by the common law courts brought with it a tendency to ascribe the distinction between penalties and liquidate damages to the intention of the parties.[2] During the nineteenth century when the will theory of contract purported to relate every aspect of a contract to the intention of the parties, such a notion inevitably gained in popularity. However, such an approach distorted the policy against penal clauses which had been developed over many centuries.

The effect of the principles developed by equity has been summarised by saying that in the determination of

> the question whether or not a stipulation should be construed as providing for a penalty or for liquidated damages the guiding principle for the courts to observe should be that of 'just compensation' for injury resulting from the breach of the contract, and the controlling object should be to place the injured party in as advantageous position as he would have occupied had his contract not been broken. So long as the contracting parties keep this principle in view the courts will very generally allow them to agree upon such a sum as will probably be the fair compensation for the breach of a contract. But when they go beyond this, and undertake to stipulate, not for compensation, but for a sum entirely disproportionate to the measure of liability which the law regards as compensatory, the court will refuse to give effect to the stipulation and will confine the parties to such actual damages as may be pleaded and proved.[3]

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1 See, for example, Astley v. Weldon (1801)2 B. & P. 346; Kemble v. Farren (1829)6 Bing. 141.

2 See, for example, the speech by counsel for the defendant in Kemble v. Farren (1829)6 Bing.141, 142. Also Jessel M.R. in Wallis v. Smith (1882)21 Ch.D.243; Lord Elphinstone v. Monkland Iron and Coal Co. Ltd. (1886)11 A.C.332.

3 Pembroke v. Caudill 6 ALR2d 1395 as quoted by Williston op. cit., Section 778.

Scots Law.

The early development of the jurisdiction against penal clauses was strongly influenced by the laws against usury. In Home v. Hepburn,[1] a case decided in 1549, the court declared that "de practica Scotiae" only such loss as was actually suffered could be recovered and not penal sums "quia sapiunt quondam usuram et inhonestum quaestum"[2]

After the Reformation the law was somewhat relaxed as is reflected by the institutional writers. Bankton said that

> /B/ecause damage and interest is frequently of most difficult estimation; therefore, in obligations to facts, it is advisable, and ordinary to adject a penalty, consisting of a liquid sum, that shall become due, upon the debtor's default...: here it is not considered, how far the creditor suffers detriment thro' non-performance; but the court of session, in such a case, would probably tax an exorbitant penalty to the just interest of the party.[3]

Stair maintained that the "Lords ex officio have power to modify exorbitant penalties, albeit they bear to be liquidate of consent of parties."[4] And Bell, writing during the height of the classical period, distinguished between two types of clauses:

> Where such penalties /in contracts ad factum praestandum/ are intended as liquidated damages, and especially where there appears to be nothing exorbitant in the stipulation, but a reasonable and fair proportion between the loss and the penalty, a court of justice will not interfere... But where the penalty is manifestly exorbitant and a penal forfeiture rather than estimated damage, a court of equity does interfere; the exorbitancy being taken in some sort as a criterion whether it be properly a penalty or conventional damage that has been stipulated.[5]

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1 (1549) Mor. 10033.

2 In this case an exception was made because the penal clause operated against an Englishman and the defendant was condemned "in odium anglorum, in favorem republicae"!

3 I,23,75.

4 V,18,3. I,10,14.

5 Commentaries, 699. See too the same effect Kames, Equity, 297.

It is thus clear that although Scots law, even in the time of Kames and later in that of Bell, had already accepted the English terminology of "penalties" and "liquidate damages" they did not necessarily bear the same meanings as in English law. Craig v. M'Beath[1] was a case in which the court was called upon to decide on the enforceability of a clause stipulating payment of £25 in the event of a breach. Lord Justice-Clerk Inglis expressed the opinion that "it is a penalty of that kind which we are bound to modify to the actual loss if duly required by the defender to do so."[2] The question in these cases, his Lordship continued, was

> whether the sum stipulated to be paid in the event of breach of contract is liquidate damage, or merely represents the general agreement that a money payment shall be made to the extent of the damage caused by the breach of contract, and I have no doubt that, in this case, this sum... is of the latter kind.[3]

His Lordship compared this case with another in which the court upheld a "penalty" as liquidate damage:

> The chief ground of our judgment in that case was, that the sum conditioned to be paid bore a clear proportion to the amount of loss sustained by the party entitled to claim it; and from that we inferred that it was the intention of the parties that the sum named should be held to be the true measure of the damage. But, in this case, there is no such proportion.[4]

It is clear that although the tendency to base the distinction between penal clauses and liquidate damages on the intention of the parties began to take root in Scots law as it did in English law it did not

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1 (1863) IM. 1020.

2 Ibid., 1022.

3 Ibid.

4 Ibid.

deter the courts from concerning themselves essentially with whether the sum stipulated was extravagant or not.

In the later case of Forrest and Barr v. Henderson[1] the question whether a sum stipulated to be paid upon breach would be enforced without modification by the court was said to depend upon whether it was "extravagant, exorbitant or unconscionable."[2] If so, the amount would be modified to correspond to the damage incurred by the creditor. Although the terms "penalties" and "liquidate damages" are used by the judges in this case their meanings are not entirely clear. It would seem, and the judgments in Craig v. M'Beath support this,[3] that "penalties" are clauses which are inserted solely to punish a party for non-performance of his obligation. When they are disproportionate to the damage caused by the breach they may be reduced. But even when a clause is classified as a genuine pre-estimate of loss it may be reduced if it stipulates for the payment of an exorbitant sum.[4]

Scots law, therefore, although it paid half-hearted lip service to the distinction between penalties and liquidate damages never, or in any case, not before the beginning of this century, regarded it as of fundamental importance. Where a sum stipulated was grossly out of proportion to the total loss which could possibly flow from the breach it could be modified to correspond more closely with the damage suffered, irrespective of whether it was a penalty or liquidate damages.

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1 (1869) 8M. 187.

2 See also Heir of John Porteous v. John Nasmith 1783 Mor.120.

3 (1863) IM.1020, 1023 and 1024.

4 (1869) 8M. 187 per Lord President Inglis. See also Lord Deas at 196, Lord Ardmillan at 199, Lord Kinloch at 201, and Lord Neaves at 202. Contra Lord Elphinstone v. Monkland Iron and Coal Co.Ltd. (1886) 11 A.C.332.

Modern caselaw:

In modern English and Scots law the question whether a sum stipulated to be paid on default will be held enforceable or not, will depend, in accordance with the dictum of Lord Dunedin in the leading case of Dunlop Pneumatic Tyre Co.Ltd., v. New Garage & Motor Co.Ltd.,[1] upon whether the court construes the pecuniary sum as a penalty, that is "a payment of money stipulated as in terrorem of the offending party" or as liquidate damages, which is defined as "a genuine covenanted pre-estimate of damage." If a clause is adjudged to be a penalty it is unenforceable, but if it is liquidate damage it will be enforced without reduction. Whether a clause falls within the one or the other category is said to depend upon construction and on the surrounding circumstances at the time that the contract was concluded and not with hindsight as of the time of breach. This is so irrespective of whether the term "penalty" or "liquidate damage" is used by the parties.

We have already alluded to the increasing tendency of courts to base the distinction between penalties and liquidate damages on the intention of the parties. Such an approach is misconceived as the judicial control exercised cannot be explained merely by construction of the contract.[2] If it were solely a question of the intention of the parties then almost every clause stipulating damage would have

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1 /1915/ A.C. 79,86.

2 See, for example, Lord Radcliffe in Bridge v. Campbell Discount Co. Ltd. /1962/ A.C.600, 624: It is "'a question not of words or of forms of speech but of substance and of things.' It cannot really depend on a point of construction..."

to be enforced as the inclusion of the term in the contract is assumed to be the expression of the parties' intention. It would be absurd to expect of the parties to agree to a clause which they never intended to be enforceable. The real inquiry of the court is therefore not what the parties intended the clause to be, but whether a clause is in fact a penalty or liquidate damages. It has been stated before that in English law this distinction was made not on the basis of any intention expressed by the parties, but because the judiciary increasingly disapproved of the inclusion of terms whose sole function was to compel performance of the contractual obligations. The enforcement of contracts they regarded as their prerogative. The terminology was taken over by Scots law but the case law shows that the terms did not necessarily have the significance that they had in English law.

The most important way in which a court can establish whether a clause is a penalty or genuine pre-estimate of loss is to determine whether the sum stipulated was clearly extravagant when compared to the greatest possible loss which could flow from the breach. If so, then the clause cannot be liquidate damage, but can only be a penalty. This approach was recognised by Lord Dunedin in the Dunlop case where he maintained that a clause "will be held to be penalty [sic] if the sum stipulated for is extravagant and unconscionable in amount in comparison with the greatest loss that could conceivably be proved to have followed from the breach."[1]

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[1] [1915] A.C. 79,87.

Although Lord Dunedin described this test as a rule of construction, judicial dicta clearly indicate that this is not so, but that the fairness of the sum stipulated vis-à-vis the estimated loss is the fundamental test by which the courts decide whether a clause is enforceable or not. None is clearer than Lord Atkinson in the Dunlop case:

> It was laid down /in Webster v. Bosanquet[1]/ that in determining whether a sum contracted to be paid is liquidated damages or a penalty, one is to consider whether the contract, whatever its language, would, at the time it was entered into, have been unconscionable and extravagant, and one which no Court ought to allow to be enforced if this sum were to be treated as liquidated damages, having regard to any possible amount of damage likely to have been in the contemplation of the parties when they made the contract.[2]

In Clydebank Engineering & Shipbuilding Co. Ltd., v. Don Jose Ramos Yzquierdo Y Castanedo,[3] a Scottish appeal to the House of Lords, the question was whether a stipulation that

> /t/he penalty for later delivery (than times specified) shall be at a rate of £500 per week for each vessel

was a liquidate damage clause or a penalty -

> whether it is, what I think gave the jurisdiction to the Courts in both countries to interfere at all in an agreement between the parties, unconscionable and extravagant, and one which no Court ought to allow to be enforced.[4]

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1 /1912/ A.C. 394 (P.C.), in which Lord Mersey said that "...whatever the expression used in the contract in describing the payment, the question must always be whether the construction contended for renders the agreement unconscionable and extravagant and one which no Court ought to allow to be enforced..."/398/. In Dingwall v. Burnett 1912 S.C. 1097, Lord Salvesen equated Scots law with English law and accepted Webster v. Bosanquet as a correct exposition of the law.

2 /1915/ A.C. 79, 95.

3 /1905/ A.C. 6.

4 Ibid., 10 per Earl of Halsbury L.C.

That this test was the true basis for the decision was reinforced by Lord Davey where he said that

> it is always open to the parties to shew that the amount named in the clause is so exorbitant and extravagant that it could not possibly have been regarded as damages for any breach which was in the contemplation of the parties, and that is a reason for holding it to be a penalty and not liquidate damages.[1]

In that case the clause was upheld by the House of Lords evidently because they regarded the sum as fair in the circumstances.

That the true test for distinguishing between penalties and liquidate damage lies in the proportionality between the sum stipulated and the greatest possible loss that could occur as a result of a breach is further strengthened by the second and third "rules of construction" which were set out by Lord Dunedin in the Dunlop case. According to the second test "/i/t will be held to be a penalty if the breach consists only in not paying a sum of money, and the sum stipulated is a sum greater than the sum which ought to have been paid."[2] The third test reads:

> There is a presumption (but no more) that it is a penalty when a single lump sum is made payable by way of compensation, on the occurrence of one or more or all of several events, some of which may occasion serious and others but trifling damage.[3]

The reason for branding such a clause as a penalty, often in the face of perfectly unambiguous language in the contract, can only be that

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1 Ibid., 16.

2 /1915/ A.C. 79, 87 citing Kemble v. Farren (1829) 6 Bing. 141.

3 Ibid., citing Lord Elphinstone v. Monkland Iron & Coal Co. Ltd. (1886) 11 A.C. 332, 342.

the sum stipulated will be greatly disproportionate to the loss caused by a minor breach.

It is conventionally stated that the fairness of a sum should be tested as of the time that the contract was concluded and not as of the time of the breach.[1] Yet it is submitted that the courts must and indeed often do take account of the actual damage that was caused by a breach. Therefore, in a case where a sum is made payable on the occurrence of different breaches, some important and other less serious, the courts will not automatically hold a clause to be a penalty. Where, for example, the breach that has actually occurred causes damage which is proportionate to the sum stipulated, the courts will attempt to construe the clause as pertaining only to such a serious breach and not to a trifling one.[2]

Damage clauses are quintessentially designed for the situation where the loss which may flow from a breach is uncertain.[3] Where that is the case the courts will generally regard the stipulated sum as fair and allow enforcement of the clause. But even here a certain amount of hindsight will be employed and if the sum is clearly disproportionate to the loss suffered it will often be adjudged a penalty.[4]

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1 See, for example Dunlop Pneumatic Tyre Co. Ltd. v. New Garage & Motor Co. Ltd. /1915/ A.C. 79, 87 and the Law Commission Working Paper No. 61, Penalty Clauses and Forfeiture of Monies Paid (1975). Contra the South African Conventional Penalties Act. No. 15 of 1962 which in section 3 provides that the sum stipulated should be compared with the "prejudice suffered" by the creditor. The Uniform Commercial Code provides in section 2-718 that "Damages for breach by either party may be liquidated in the agreement but only at an amount which is reasonable in the light of the anticipated or actual harm caused by the breach."

2 Webster v. Bosanquet /1912/ A.C. 394.

3 See Dunlop Pneumatic Tyre Co.Ltd. v. New Garage & Motor Co.Ltd. /1915/A.C. 79, 88 per Lord Dunedin.

4 Ford Motor Co. (England) Ltd. v. Armstrong /1915/ 31 T.L.R. 267.

The jurisdiction against penalties is an important instance of the courts' direct attack on unfair contract terms. The central reason why the courts intervene in the case of penalties, and also in the case of forfeitures generally, is the realization that a person subjected to a penalty would, if it was enforced, lose the sum stipulated without adequate return and without a breach of duty on his part commensurate in value to the money paid.[1] Although the courts set out to protect the expectations created by the contract, they are not prepared to award the aggrieved party more than he would have received had the contract been performed and thereby sanction a grossly unequal exchange of values. Unlike many other areas where the courts scrutinise the fairness of contracts, there is here no attempt to relate the clause to some defect in the process of contracting and there is no inquiry as to whether the debtor had freely and consciously agreed to the term. The mere disproportion between the sum stipulated and the loss caused by the breach is sufficient reason to strike down the clause. This practice is undoubtedly the result of the tendency to see penalties as penal by nature and, therefore, inherently worthy of disapproval.

The reason why the courts apply a fairness test to damage clauses is thus the result of special historical factors and this may be a reason why the courts have been so reluctant to extend the principles applied in the case of penalties to other contract terms which, although they may differ from penalties in form, are essentially

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[1] Williston, op. cit. section 769.

similar in character. Except for a few isolated examples the courts have shown little inclination to give a wide definition to the concept of a penalty so as to include such other unfair terms.

Several other provisions such as acceleration clauses[1] and discounts for prompt payments[2] resemble penalties in that they serve to pressurise a debtor into performance. In addition, they may also resemble penalties in that they stipulate for the payment or forfeiture of a sum which is much greater than the loss which a breach would cause to the creditor. Yet they are not subject to the same principles as penalties and are generally enforceable. The scope of the law relating to penal clauses is further limited in that it applies only where a sum becomes payable on a breach of contract. Where a term stipulates that a payment should be made on the occurrence of some event other than a breach that provision will not be affected by the law as to penal clauses and will therefore be generally enforceable.[3]

The problem is even more acute where the clause stipulates for payment in various situations, one of which is a breach. An example of this is the "minimum payment" clauses often found in hire-purchase contracts. This provides that when the contract is prematurely determined the hirer must bring his payments up to a certain minimum. It also specifies various circumstances in which

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1 See Protector Loan Co. v. Grice (1880) 5 Q.B.D.529. Acceleration clauses are said to accelerate a party's liability, but not to increase it.

2 If the discount is unfairly large it may indicate that the smaller sum was the real debt, and the larger sum merely a penalty.

3 See for example Alder v. Moore [1961] 2 Q.B. 57.

the contract may be so determined. Where the hirer has committed a breach and the owner subsequently terminates the agreement the sum which becomes payable may be regarded as penal[1] if it is out of proportion to the loss incurred by the owner as a result of the breach. If, however, the hirer, without committing a breach, merely exercises a legal right to return the goods, the courts are powerless to intervene and the hirer will be forced to pay any amount which may be outstanding on the stipulated minimum irrespective of the loss suffered by the owner as a result of the early determination of the contract.[2]

The injustice of this has been frequently recognised by the courts and in Bridge v. Campbell Discount Co.Ltd., Lord Denning was moved to say:

> Let no-one mistake the injustice of this. It means that equity commits itself to this absurd paradox: it will grant relief to a man who breaks his contract but will penalise the man who keeps it... It is beyond doubt oppressive and unjust.[3]

Similar sentiments have been expressed in Scotland where the same paradox is to be found.[4]

In the Bridge case relief was eventually granted by the indirect means of construing the hirer's letter informing the owner

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1 See for example Cooden Engineering Co. v. Stanford [1953] 1 Q.B. 86; Lamdon Trust Ltd. v. Hurrell [1955] 1 W.L.R. 391.

2 English law: Associated Distributors Ltd. v. Hall [1938] 2 K.B.83; United Dominion's Trust (Commercial) Ltd. v. Ennis [1968] 1 Q.B.54. Scotland: Bell Bros. v. Aitken 1939 S.C.577, followed in Granor Finance Ltd. v. Liquidator of Eastore Ltd. 1974 S.L.T. 296; Mercantile Credit Co.Ltd. v. McLachlan 1962 S.L.T. (Sh.Ct.) 58.

3 [1962] A.C. 600, 629.

4 Mercantile Credit Co.Ltd. v. McLachlan 1962 S.L.T. (Sh.Ct.)58; Mercantile Credit Co.Ltd. v. Brown 1960 S.L.T. (Sh.Ct)41.

that he could not continue payments and therefore wished to determine the contract - a right conferred on him by the contract - as a breach and not the mere exercise of an option stipulated in his favour and the court, by so doing was able to pronounce the minimum payment to be a penalty and not liquidate damage. Lord Denning was also of the opinion that the hirer could be relieved on the ground of existing principles of equity, but this idea did not gain the acceptance of his fellow Lords. The technique used by the majority to grant relief to the party in that case was employed in earlier cases[1] and has also been used since then.[2] Although it facilitates a fair result it involves such spurious reasoning that it cannot be accepted.

Section 100(1) of the Consumer Credit Act 1974 now provides that a debtor under a regulated hire-purchase agreement (or regulated conditional sale) is able to terminate an agreement prematurely on condition that he pays the difference between the sums already paid or payable by him and one-half of the total price. And section 100(3) gives the court the power to order repayment of a smaller sum if that would adequately compensate the owner for his loss. Where, however, the Consumer Credit Act does not apply the situation will still be governed by the common law.

Penalty clauses were discussed by the Law Commission in a Working Paper in 1975.[3] The Commission came out in favour of

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1 Mercantile Credit Co.Ltd. v. Brown 1960 S.L.T. (Sh.Ct.) 41.

2 Bowmaker (Commercial) Ltd. v. MacDonald 1965 S.L.T. (Sh.Ct.) 33.

3 Working Paper No. 61, Penalty Clauses and Forfeiture of Monies Paid (1975).

retaining the present distinction between penalties and genuine pre-estimates of loss[1] but they were of the opinion that relief should also be possible where a clause with a penal effect came into operation without a breach of contract.[2] The Commission accordingly felt that the rules as to penalties should apply "wherever the object of the disputed contractual obligation is to secure the act or result which is the true purpose of the contract."[3] This recommendation, while it would improve the situation slightly, is so cumbersome that it will most likely lead to further problems of interpretation. To date this recommendation has not been acted upon.

(iv) Forfeiture of Monies Paid[4]

The question whether a party in breach may recover payments made by him under a contract is said in both English and Scots Law, to depend upon the intention with which the payment was made. If it was paid as a deposit, that is "a guarantee that the contract shall be performed",[5] it cannot be recovered unless there is a

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1 Ibid., 51-52.

2 Ibid., 51.

3 Ibid., 18-19.

4 See generally the Law Commission Working Paper: Penalty Clauses and Forfeiture of Money Paid No. 61, 1975, 36 et seq; Treitel, Law of Contract 742-745; Goff and Jones, The Law of Restitution, 380-386.

5 Howe v. Smith (1884) 27 Ch.D.89, 95. See also Roberts & Cooper v. Salvesen 1918 S.C. 794, 806 per Lord President Clydesdale where he says that the law in Scotland is similar to that in England. Also Commercial Bank of Scotland v. Beal (1890) 18 R. 80, 85. Reid v. Campbell 1958, S.L.T. (Sh.Ct.) 45.

specific provision in the contract to that effect.[1] On the other hand, where money has been paid as part of the total purchase price it may be recovered unless it is prohibited by a valid forfeiture clause in the contract. The recovery will, however, be subject to a cross-claim for damages.[2]

The forfeiture of a deposit or part payment differs from the payment of a penal sum only in respect of the time at which they become payable - the former before the breach of contract has occurred and the latter after the breach - and where a deposit which ought to have been paid, but has not, is claimed after the breach the distinction is even less real.[3] The forfeiture of a deposit or part payment can, like the payment of a penal sum, operate in terrorem of a party, and may also, and indeed frequently does, have no relation to the damage actually incurred by the innocent party as a result of the breach. The forfeited deposit or part payment may therefore be as "extravagant, exorbitant and unconscionable" as any penalty. Despite similarities in nature and effect between deposits and penal clauses the courts have for many years considered the equitable jurisdiction established in respect of penal clauses as irrelevant, even by analogy, to the forfeiture of deposits. The formal origin of this harsh approach to deposits is generally stated to be Howe v. Smith,[4] but in substance it is merely a manifestation of the

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1 Howe v. Smith, (1884) 27 Ch.D. 89.

2 See Dies v. British and International Mining and Finance Corporation [1939] 1 K.B. 724, 744. Also Hinton v. Sparkes (1868) L.R. 3 C.P. 161, 165.

3 See Hinton v. Sparkes (1868) L.R. 3 C.P. 161; Dewar v. Mintoft [1912] 2 K.B. 373; Lowe v. Hope [1969] 3 All E.R. 605.

4 (1884) 27 Ch.D. 89.

principle of freedom of contract. There are, nevertheless, a few cases in which it seems as if the law as to penal clauses has been applied to the forfeiture of deposits. In Public Works Commissioners v. Hills[1] a contract for the construction of a railroad provided that a security deposit of £50,000 should be forfeited if the contractors failed to complete the work on time. The Privy Council was of the opinion that the forfeiture clause was penal and therefore that the deposit should be repaid to the contractors. If the law in respect of penal clauses is to be applied to a provision for the forfeiture of a deposit such a forfeiture would of course be enforced where the sum deposited is not grossly disproportionate to the greatest possible loss that could flow from the breach.[2] The cases where the law as to penalties have been applied to deposits are, however, exceptions and the continued distinction between penalties and deposits remain curious and unjustified.

Judicial intervention has occurred most frequently in contracts of sale by instalments where the purchaser, as a result of default in a single instalment stands to forfeit all the money already paid, irrespective of the loss incurred by the seller. It has been firmly established through a series of judgments that in such a case the courts can at least relieve a purchaser who is willing and able to perform by granting him an extension of time for payment or by ordering the seller to repay the forfeited instalments in a case

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1 /1906/ A.C. 368.

2 Pye v. British Automobile Commercial Syndicate Ltd. /1906/ 1 K.B. 425.

where the purchaser was willing and able to perform but where specific performance could for some valid reason not be decreed.[1] The development of a general jurisdiction of relief has been seriously hampered by certain judges interpreting those decisions that have come out in favour of relief from forfeiture in the most restrictive way possible.[2] Notwithstanding this tendency, there are passages in the judgments which suggest a wider perspective, for example by treating part payments as akin to penal clauses.

Whether any relief other than an extension of the time for payment will be given is uncertain. There are, however, strong dicta in Stockloser v. Johnson[3] that equity will provide relief on a much wider basis. In that case the buyer of quarrying machinery brought an action against the seller for repayment of the already paid instalments, alleging that their retention amounted to a penalty from which he was entitled to be relieved. The Court of Appeal (Somervell, Denning and Romer L.JJ.) unanimously refused relief, Somervell and Denning L.JJ. on the ground that it was not in the circumstances unconscionable that the seller retained the sum. Romer L.J. on the other hand, maintained that equity had never interfered with contracts merely because they were improvident.

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1 See generally, In re Dagenham (Thames) Dock Co., Ex parte Hulse (1873)8 Ch.D.10 ; Kilmer v. British Columbia Orchard Lands, Ltd. [1913] A.C. 319; Steedman v. Drinkle [1916] 1 A.C. 275; Mussen v. Van Diemen's Land Co. [1939] Ch. 238.

2 Especially Farwell J. in Mussen v. Van Diemen's Land Co. [1939] Ch.238.

3 [1954] 1 Q.B. 476.

> There is, in my judgment, nothing inequitable per se in a vendor, whose conduct is not open to criticism in other respects, insisting upon his contractual right to retain instalments of purchase money already paid.[1]

His Lordship declared that before rescission a court will intervene only to give a purchaser in default who is willing and able to proceed with the contract, an extension of time for payment and after rescission the defaulting party will receive no relief unless there was fraud, sharp practice or some other unconscionable conduct on the part of the seller.[2] Romer L.J. did not explain what he meant by "sharp practice" or "unconscionable conduct", but from his general view of the law it seems clear that these terms refer exclusively to defects in the bargaining process and not to any substantive features of the contract.

The majority of the court thought that both equity and the earlier caselaw indicated a wider jurisdiction than that intimated by Romer L.J. Denning L.J. specifically declared that while a readiness and willingness to perform the contract is necessary for specific performance or relief from forfeiture of leases, it is not a prerequisite for relief from forfeiture of sums paid.[3] Denning L.J. also drew a distinction between the principles relevant in this case and those that operate to relieve a party from paying a penalty. In the latter case relief is granted because the court will not sanction an act of oppression. Here the seller only wishes to keep money which already belongs to him and which he acquired not by

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1 Ibid., 501

2 Ibid.

3 Ibid., 491.

extortion or oppression, but as part of the purchase price.[1] A party will only be allowed to recover money paid, irrespective of whether it was a "part payment" or a "deposit", if two conditions are fulfilled:

> /F/irst, the forfeiture clause must be of a penal nature, in this sense, that the sum forfeited must be out of all proportion to the damage, and, secondly, it must be unconscionable for the seller to retain the money... /I/n a proper case there is an equity of restitution which a party in default does not lose simply because he is not able and willing to perform the contract. Nay, that is the very reason he needs the equity. The equity operates, not because of the plaintiff's default, but because it is in the particular case unconscionable for the seller to retain the money. In short, he ought not unjustly to enrich himself at the plaintiff's expense. The equity of restitution is to be tested, I think, not at the time of the contract but by the conditions existing when it is invoked.[2]

Whether equity is to give relief depends upon all the circumstances of a particular case and is not to be decided by looking only at the contract terms.

The central theme of the majority judgments, namely that a clause stipulating for the forfeiture of monies paid, may be declared invalid if it is inequitable in the circumstances, has been widely welcomed. Yet the judgments, especially that of Denning L.J., raise a number of questions which they do nothing to resolve. It is clear from the judgment of Denning L.J. that a gross imbalance between the sum forfeited and the damage incurred, although a cardinal factor, is not in itself sufficient to render the forfeiture clause inequitable - the retention of the instalments or deposit must also be "unconscionable". But what factors or circumstances will make

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1 Ibid., 488-489.

2 Ibid., 490, 492.

the retention unconscionable, we are not told. It is possible that this requirement relates not to substantive unconscionability but to unfairness in the exercise of the right to retain the money. Perhaps the retention must be "oppressive" as penalties are supposed to be. But why is a penalty described as oppressive only because of a gross disproportion between the penal sum and the damage, and a forfeiture of money paid, under similar circumstances, not? Despite his Lordship's assertions it is doubtful whether the distinction between penalties and forfeitures of money paid is real. It is also interesting to note that the only examples given by Denning L.J. of situations where the courts would declare a forfeiture clause inequitable are merely cases where there was great disparity between the amount of the instalments and the damage, without more.[1] It is in fact extremely doubtful whether in this field the requirement of "unconscionability" adds in any significant way anything to the requirement of penality. It seems nothing more than a ritual incantantion that contracts cannot be refused enforcement only because of an unequal exchange of values. This view of the law is reinforced by the decision in the case. There is no indication in the judgments that there was any gross disparity between the sum forfeited by the buyer and the damage suffered by the seller. Denning L.J. accepted the assertion by the judge a quo that the forfeiture clause was penal, but the latter only regarded it as such because it was not liquidate damages in the orthodox sense.[2] In fact the majority judgments gave

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1 Ibid., 491, 492.

2 See the judgment of Somervell L.J. 483.

no substantial reasons for their finding that the forfeiture clause was equitable. Under these circumstances there must be a strong suspicion that this was done merely because there was no great disproportion between the values exchanged.

The law as espoused by Denning and Somervell, L.JJ. in the Stockloser case was not followed in Galbraith v. Mitchenall Estates Ltd.[1] where Sachs J. refused to allow recovery of instalments paid under a contract of hire despite the fact that he described the terms of the contract as "hideously harsh". His Lordship instead accepted the views of Romer L.J. in the Stockloser case as more in accordance with established authority. Sachs J. was also impressed by "the difficulties which would face a court if there had to be some substitution of terms."[2]

Many of the situations discussed above will now be covered by the provisions of the Consumer Credit Act 1974. For example, in terms of section 100(1) a debtor under a regulated hire-purchase (or regulated conditional sale) agreement who has prematurely terminated the agreement will now be liable to pay the difference between the sums already paid or payable by him and one-half of the total price. And section 100(3) gives the court the power to order payment of a smaller sum if that would be equal to the loss of the creditor.

The refusal of the courts to grant relief from the unfair forfeiture of a deposit was criticised by the Law Commission in its

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1 [1964] 3 W.L.R. 454.

2 [1964] 2 All E.R. 653, 658.

Working Paper on the subject. The Commission suggested instead that forfeiture of a deposit should only be allowed where it is a "genuine pre-estimate" of the loss likely to be caused by a breach.[1] But as they realized that such a rule would, in most cases, lead to the invalidation of the right to forfeit a deposit, forfeiture clauses in land transactions were specifically excluded from the scope of the proposal.[2]

Equity's Doctrine against Forfeitures - Summary

From an early time forfeiture and penal clauses, stipulating for the loss or payment of a certain sum in the event of non-performance of a party's promises, functioned as forms of security. The sums so required to be paid by the promisor were often much greater than the loss which non-performance would have caused the promisee. The courts, influenced by the standard of fair exchange which had filtered through from the usury laws, soon began to give relief from such forfeiture and penal clauses on account of the unequal exchange which they stipulated for. Whenever the promisee could be sufficiently compensated for the loss occasioned by the promisor's breach the forfeiture clause was struck down.

Inevitably specific rules began to develop in each area where the general principle against forfeitures was applied. These rules were, especially during the nineteenth century often applied

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1 Law Commission, op. cit., 48-49.

2 Ibid.

in such a mechanistic and rigid manner that otherwise fair contract provisions were struck down.

Lately, a more flexible approach on the part of the courts has become discernible, especially in the areas of mortgages and leases. The fairness of the forfeiture clause is still regarded as of paramount importance, but the fairness can only be judged with reference to all the surrounding circumstances.

The principle that a penal clause would not be allowed to stand unless fair was also a principle which Scots law had adopted in consequence of the influence of the usury laws. Until the late nineteenth century it was generally accepted that a penal sum could be modified so as to accord more closely with the loss which was likely to be caused by a breach. In respect of the forfeiture of monies paid Scots law has largely followed English law. The rules in respect of the equity of redemption and forfeiture of leases are, because of differences between Scots law and English law not relevant to the former.

(b) Specific Performance

Specific performance is a discretionary equitable remedy and the principle is well established that a court will grant it only where it is fair and just to do so.[1] The discretion vested in the courts is not arbitrary, but is said to be exercised in accordance

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[1] See for example the statement by Lord Hardwicke L.C. in Buxton v. Lister (1746) 3 Atk.383, 386 that "/n/othing is more established in this court, than that every agreement in respect of which specific performance is decreed, ought to be certain, fair, and just in all its parts."

with settled principles.[1] The decision to withhold or decree specific performance may only be made after all the circumstances of the case have been taken into account.

Specific performance may be refused where it will cause hardship to the debtor or if the contract itself is unfair or has been unfairly obtained. The unfairness must be present when the contract is concluded. The court will not, for example, withhold specific performance merely because a seller, initially well satisfied with her bargain, later discovered that she could have got more for the sale of her property.[2] It is furthermore said that the unfairness need not be so serious as to constitute equitable fraud:[3] a court may refuse specific performance and at the same time not set the contract aside, but leave the creditor free to claim damages at law.[4] In Day v. Newman the court expressed this idea as follows:

> I think there are no grounds on which I can set the contract aside; for neither side have a right to complain of a bargain made so deliberately as this was. The party has no right to ask the Court to prevent the consequences of his own solemn act; but on the other hand, most certainly this is too hard a bargain for the Court to assist in.[5]

This is a curious distinction: in the first place, except where there is some circumstance which renders specific performance,

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1 Lamare v. Dixon (1873) L.R. 6 H.L. 414, 423; Conlon v. Murray /1958/ N.I. 17, 25.

2 Collier v. Brown (1788) 1 Cox 428, 431. Also Western v. Russell (1814) 3 V. & B. 188.

3 Young v. Clerk (1720) Pr. Ch. 538; Kemeys v. Hansard (1815) Coop.G.125.

4 Hick v. Phillips (1721) Pr. Ch.575; Savage v. Taylor (1736) Cas.t.T. 234; Mortlock v. Buller (1804) 10 Ves. 292.

5 (1788) 2 Cox 77, 83.

but not the payment of damages, unduly hard on the debtor, one would expect a contract which is adjudged to be too unfair in its terms to perform specifically to be similarly too unfair to provide a basis for a claim of damages; secondly, it is doubtful whether there are in fact many circumstances which will provide a ground for refusing specific performance and not at the same time amount to equitable fraud, especially as equitable fraud was purposely never clearly defined lest ways should be found to circumvent it.

The rule that specific performance may be refused without also setting the contract aside, but leaving the creditor to claim damages for breach at common law, has been severely criticised by commentators.[1] According to Atiyah[2] it dates from a period when the amount of damages which would be awarded for breach was in the discretion of the common law jury. The result was that if a debtor complained that he had contracted to pay an excessive price the jury would mitigate damages to accord more closely with a fair exchange.[3] As the circumstances which earlier justified the rule have since disappeared it has become an anachronism.

A distinction between the circumstances which lead to a refusal of specific performance and those which constitute equitable fraud will only be

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1 See, for example, R.A. Newman, Renaissance of Good Faith in contracting in Anglo-American Law (1969) 54 Cornell L. Rev. 553, and the writers there cited.

2 Atiyah, The Rise and Fall of Freedom of Contract, 148-149.

3 Atiyah, op. cit., cites James v. Morgan (1665) 1 Lev. 111 and Thornborow v. Whitacre (1704) 2 Ld. Ray 1164 in support. These cases are in fact often described as dealing essentially with the question of damages.

justified if specific performance were refused solely because the terms of a contract were unfair or the consideration inadequate. But the attitude of the courts toward the question whether inadequacy of consideration is a ground for refusing specific performance has been ambivalent. On the one hand there is a large number of cases in which it has been stated that inadequacy by itself is not a sufficient reason for withholding specific performance and that where contracts are freely concluded they will not be interfered with.[1] On the other hand there is the declaration by Lord Eldon L.C. in Coles v. Trecothick that inadequacy of consideration will, by itself, constitute a bar to specific performance where it "is such as shocks the conscience, and amounts in itself to conclusive and decisive evidence of fraud in the transaction."[2] It will, however, be strange if, in such a case, the courts merely deny specific performance without also setting the contract aside on the ground of fraud.

Despite the many assertions to the contrary it is clear that some degree of inadequacy of consideration per se will lead to a refusal of specific performance.[3] But what degree of inadequacy will be sufficient is uncertain. In Abbot v. Sworder[4] a person sold his farm worth £3,500 to his solicitor for £5,000. Although Knight

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1 See Keen v. Stuckely (1721) Gil. 155, where the Lords were divided on the question; Copis v. Middleton (1818) 2 Madd. 410; Western v. Russell (1814) 3 V. & B. 188.

2 (1804) 9 Ves. 234. Also Morse v. Royal (1806) 12 Ves. 355.

3 Young v. Clerk (1720) Pr.Ch. 538, 540; White v. Damon (1802) 7 Ves. 30;

4 (1852) 4 De G. & S. 448.

Bruce V.C. recognised that mere excess of price could be a sufficient ground for refusing specific performance he did not think that it would have that effect in this case as the solicitor "must be supposed to have been not incapable of attending to his own interests."[1] In Vaughan v. Thomas[2] a contract for the purchase of an annuity worth nine years' purchase for a sum equal to five years' purchase was labelled "a very unconscientious bargain" and specific performance refused.

The truth, however, is that the inadequacy of consideration seldom stands alone - where there exists striking inadequacy of consideration the courts will more often than not find an accompanying factor which will, in conjunction with the inadequacy, justify refusal of specific performance. Such additional factors may of course take various forms. It may, for example, be that the creditor obtained the contract by "surprise",[3] or as a result of ignorance as to the value of goods on the part of the debtor.[4] Specific performance will also be refused where the creditor took unfair advantage of the debtor as a result of their unequal bargaining position.[5] Such inequality may be caused by various factors such as the financial

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1 Ibid., 456.

2 (1783) 1 Bro. C.C. 556.

3 Walters v. Morgan (1861) 3 D.F. & J. 718.

4 Young v. Clerk (1720) Pr. Ch. 538; Hick v. Phillips (1721) Pr. Ch. 575; Falcke v. Gray (1859) 4 Drew. 651.

5 Conlon v. Murray [1958] N.I.17; Buckley v. Irwin [1960] N.I. 98, in which the court not only refused specific performance, but also set the contract aside notwithstanding the fact that the latter was not claimed in the pleadings.

distress[1] or habits of intoxication of the debtor.[2]

On the other hand, specific performance may also be refused on the ground of inadequacy of consideration where the character of the parties to the transaction is quite unimpeached. In Mortlock v. Buller[3] an estate worth £33,000 was sold for £26,000 as a result of negligence on the part of the sellers' agent. Lord Eldon refused specific performance although he was not prepared to set the transaction aside.

Specific performance may, furthermore, be refused where it would create hardship to the debtor which is out of proportion to the benefit which specific performance would have for the creditor. The courts often use this rule to deny enforcement of a contract on the basis of inadequacy of consideration. In Hick v. Phillips,[4] where, because of a misconception about the value of the land which he had bought, the debtor was obliged to pay more than the true value, the court said that the hardship to the debtor which prevented the granting of specific performance arose from the fact that an "over value" was being required from the debtor.

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1 Kemeys v. Hansard (1815) Coop. G. 125; Falcke v. Gray (1859) 4 Drew 651.

2 Bell v. Howard (1742) 9 Mod. 302.

3 (1804) 10 Ves. 292.

4 (1721) Pr. Ch. 575.

(c) Equitable or Constructive Fraud[1]

The various manifestations of fraud were set out by Lord Hardwicke L.C. in the leading case of Earl of Chesterfield v. Janssen:[2]

> This court has an undoubted jurisdiction to relieve against every species of fraud. 1. Then fraud, which is dolus malus, may be actual, arising from facts and circumstances of imposition; which is the plainest case.[3] 2. It may be apparent from the intrinsic nature and subject of the bargain itself; such as no man in his senses and not under delusion would make on the one hand, and as no honest and fair man would accept on the other; which are unequitable and unconscientious bargains. A 3d kind of fraud is, which may be presumed from the circumstances and condition of the parties contracting ... it is wisely established in this court to prevent taking surreptitious advantage of the weakness or necessity of another: which knowingly to do is equally against the conscience as to take advantage of his ignorance: a person is equally unable to judge for himself in one as the other. A 4th kind of fraud may be collected or inferred ... from the nature and circumstances of the transaction, as being an imposition and deceit on the other persons not parties to the fraudulent agreement...[4] The last head of fraud, on which there has been relief, is that, which infects catching bargains with heirs, reversioners, or expectants, in the life of the father, &c., against which relief always extended. These have been generally mixed cases, compounded of all or several species of fraud; there being sometimes proof of actual fraud, which is always decisive. There is always fraud presumed or inferred from the circumstances or conditions of the parties contracting; weakness on one side, usury on the other, or extortion or advantage taken of that weakness. There has been always an appearance of fraud from the nature of the bargain.[5]

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1 See generally, Sheridan, Fraud in Equity.

2 (1751) 2 Ves. 125.

3 Actual fraud falls outside the scope of this study: see Introduction.

4 Frauds on third parties will not be discussed in this study. This type of fraud referred mainly to abuses which were common in the eighteenth century but have now either fallen into disuse or are held void as being against public policy. The most important of these were marriage brokage contracts: see Keeton and Sheridan, Equity, 352-353.

5 (1751) 2 Ves. 125, 155-157.

The perception of equity's jurisdiction against unfair contracts[1] in terms of fraud first gained wide circulation in the eighteenth century. Despite the existence of some cases in which fraud was invoked as a basis for the decision, the reports of cases before the middle of the eighteenth century are generally brief and uninformative as to the grounds on which the courts proceed and it is doubtful whether one can postulate any single uniform principle on which relief was granted other than that the transactions involved were regarded either as evasions of the usury statutes then in force or as contrary to the spirit of the usury laws.[2]

The practice of basing the jurisdiction on fraud has persisted for a long time and examples can be found even in the twentieth century where fraud is still ritualistically invoked by the courts as a ground for relieving a party from an unfair contract. Despite the surprising tendency of the courts in the late nineteenth century to base their decisions more directly on the inequality between the parties, coupled with the unfairness of the exchange, the initial subsumption under fraud left its imprint on the outward aspects of the jurisdiction, not least on the terminology employed by the judges. It is thus necessary to look briefly at the general nature of equitable fraud and its implications for the jurisdiction developed by the

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1 Although most of the cases reviewed involve contracts in which there is an exchange of values there are some in which the transaction in question takes the form of gifts and voluntary conveyances. To include these the term "contract" as used here will refer to all consensual transactions.

2 Bellot, The Legal Principles and Practice of Bargains with Moneylenders, 111.

Chancery courts against unfair contracts, before embarking on a more detailed study of the various manifestations of fraud.

Equitable or constructive fraud was the vehicle by means of which the Chancery courts effected a compromise between competing values, on the one hand the principle that relief should be given from a contract which violated the standard of fair exchange and, on the other, the "classical" principle that where a contract was freely consented to it should be enforced no matter how substantively unfair it is. The conflict between these two principles was, of course, symptomatic of an even deeper doctrinal clash between the view that contractual liability depended upon substantial justice and the classical theory of contract which proclaimed that the entire contract, as well as contractual liability, derived from the intention of the parties. Although the latter conception had by the beginning of the nineteenth century become generally accepted, it, and the liberal individualism from which it sprung, did not suddenly burst upon the scene then. The transition from the earlier conception of contract to the classical model took place throughout the eighteenth century and even in the late seventeenth century notions which were later to become cardinal principles of freedom of contract, could be found. Neither was there a smooth and gradual movement from one doctrine to the other: the eighteenth century, and for that matter also the late seventeenth century, are full of conflicting judicial dicta about the relevance of unfairness in contracts.

Throughout this period the notion that contracts should be fair and the idea that all contracts freely assented to should be enforced, existed uneasily side by side. The law in respect of unfair contracts was therefore a mixture of ideas taken

from both competing theories. Nevertheless, it was clear that throughout the eighteenth century the consensualism that was to earmark the classical theory of contract, was steadily gaining ground.

The practice of setting aside unfair bargains arose because the Chancery courts, still greatly influenced at the end of the seventeenth century by the standards of contractual fairness set by the concept of usury, disapproved of a grossly unequal exchange. However, even then, judges were astute enough to realize that to give relief from contracts on the sole ground of inadequacy of consideration would be harmful to the growing commercial activity that was taking place at the time. In addition the courts, from the start of the equitable jurisdiction, refused relief from an unfair bargain which was the result of mere folly or extravagance on the part of the party claiming such relief. A bad bargain which had been voluntarily entered into by a party who suffered from no bargaining handicap which the court regarded as relevant, was not set aside. Of one such transaction Lord Nottingham L.C., after having admitted that the terms were harsh, said:

> Nevertheless, there being no surprise or circumvention of the plaintiff, but these being voluntary foolish bargains of his own making, I saw no reason for the Chancery to interpose.[1]

And in 1741 Lord Hardwicke L.C. expressed the principle thus:

> It is not sufficient to set aside an agreement in this court to suggest weakness and indiscretion in one of the parties who has engaged in it: for supposing it to be in fact a very hard and unconscionable bargain, if a person will

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[1] Pawlett v. Pleydell (1679) Selden Society, Vol. 79. Case 935. Yet Lord Nottingham did persuade the parties to a compromise.

> enter into it with his eyes open, equity will not relieve him upon this footing only, unless he can shew fraud in the party contracting with him, or some undue means made use of to draw him into such an agreement.[1]

These cases illustrate that a party who was free from any of the bargaining handicaps which Chancery recognised and who entered into the contract without regard to the level of exchange stipulated in it, would receive no assistance from the courts if he later sought to have the contract set aside. When, therefore, a person so contracting is for reasons of expediency described in this work as having entered into a contract "freely and with appreciation of the level of exchange stipulated in the contract", or "wittingly and willingly", it must not be taken to imply merely that misrepresentation, duress or mistake was absent. The Chancery courts when referring to a person having concluded a contract "freely", meant thereby not only that misrepresentation, duress or mistake was absent, but also that the party did not suffer from any of the bargaining handicaps which will be examined later in this section. Neither must the phrases be taken to imply that where the courts did intervene they did so because a party made the agreement "involuntarily" or that his consent was defective. The truth is that in this context the courts seldom focussed on the quality of consent as such, primarily because there was no need to do so in the seventeenth and eighteenth centuries. This was so despite the fact that in the nineteenth century the problem of undue influence came

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[1] Willis v. Jernegan (1741) 2 Atk. 251-252.

to be discussed largely in terms of whether the party's will had been free. The modern practice to relieve from agreements only where a party's consent was defective developed as a result of the rise of freedom of contract. The Chancery courts, on the other hand, recognised that some contractual parties were, because of their peculiar circumstances, liable to be imposed upon and they were therefore prepared to grant relief to such parties where it was found that they had in fact been imposed upon. Chancery intervened because they generally disapproved of unfair bargains and more specifically because of a protective policy towards certain contractual parties. It was therefore unnecessary to postulate defective consent as a prerequisite for judicial intervention.

In order to prove "imposition" it was initially required in some cases that misconduct on the part of the defendant be shown. Soon, however, imposition came to be inferred from the fact that an unfair bargain had been concluded with a party who was economically weak, necessitous or generally unable to protect himself in the process of contracting. This practice was followed in equity throughout the first half of the eighteenth century. Although the need to prove imposition by showing sharp practice or misconduct on the part of the defendant had been dispensed with, the term itself was retained.

In Earl of Chesterfield v. Janssen[1] Lord Hardwicke consolidated the various branches of equity's jurisdiction against unfair contracts

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[1] (1751) 2 Ves. 125.

under the head of equitable fraud. The nature of the jurisdiction, however, remained unchanged. Although Lord Hardwicke used the phrase "taking advantage of" instead of the term "imposition" it was clear that fraud could be found even where the conduct of the party who benefited from the contract was morally blameless. It was simply presumed from the inequality of the bargain coupled with the inequality between the parties, that the stronger had taken advantage of the weaker and therefore that the bargain was tainted by fraud.

Restating the jurisdiction in terms of fraud did not mean that thenceforth the courts were to approach the problem of unfair contracts through the quality of a party's consent. "Fraud", as Lord Chancellor Selborne made clear in Earl of Aylesford v. Morris, "does not here mean deceit or circumvention; it means an unconscientious use of the power arising out of /the/ circumstances and conditions /of the parties contracting/"[1] All those transactions "in which the Court is of the opinion that it is unconscientious for a person to avail himself of the legal advantage which he has obtained"[2] were regarded as tainted by equitable fraud. The formulation of the jurisdiction in terms of fraud gave the Chancery judges the opportunity to intervene in unfair contracts without the danger of being condemned as the destroyers of bargains.

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1 (1873) L.R.8 Ch. App. 484, 491; See also the discussion of constructive fraud by Lord Haldane L.C. in Nocton v. Lord Ashburton /1914/ A.C. 932.

2 Torrance v. Bolton (1872) L.R.8 Ch.App. 118, 124.

Equitable fraud was thus an enormously important weapon in Chancery's armoury against unfair contracts. It was purposely undefined and unlimited lest "the jurisdiction ... be cramped, and perpetually eluded by new schemes which the fertility of man's invention would contrive."[1]

It is now necessary to look more specifically and in greater detail at the various manifestations of equitable fraud as set out by Lord Hardwicke in Earl of Chesterfield v. Janssen.

(i) Fraud which is apparent from the nature and subject of the contract itself

We have seen that mere inadequacy of consideration was not a sufficient ground for setting aside a contract in the Chancery courts.[2] But such a principle did not stand unqualified: it meant only that not any inadequacy of consideration would serve as a basis for relief from a contract. If the inadequacy was gross it would give rise to a presumption of fraud. Lord Chancellor Hardwicke recognised this when he said in Earl of Chesterfield v. Janssen that there was a type of fraud which might be apparent from the intrinsic nature and subject of the agreement itself, "such as no man in his senses and not under delusion would make on the one hand, and as no honest and fair man would accept on the other."[3]

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1 Lord Hardwicke in a letter to Lord Kames: Yorke, Life of Lord Chancellor Hardwicke, II,550, 554 as cited by Yale, Nottingham's Chancery Cases, 73 Selden Society, xci.

2 Ante, 21.

3 (1751) 2 Ves. 125, 155.

In Drought v. Eustace[1] Lord Chancellor Hart summed up the true nature of this practice as follows:

> ... /I/nadequacy of price is not of itself sufficient, but the Court has got at it by indirect means - it has been astute, as it is said to infer fraud from inadequacy, so as to raise it indirectly into a ground for relief.[2]

Lord Hardwicke's formulation did not fall on deaf ears and in Gwynne v. Heaton,[3] Lord Thurlow L.C., after first stating that

> /a/n inadequate consideration is not alone sufficient to vitiate the contract; although in order to do so, the consideration must be inadequate; where it is sold for a sum grossly inadequate, the Court has never suffered it to stand,[4]

continued in the same vein as Lord Hardwicke L.C.:

> To set aside a conveyance, there must be an inequality so strong, gross, and manifest, that it must be impossible to state it to a man of common sense, without producing an exclamation at the inequality of it.[5]

His Lordship, however, added the following proviso:

> If parties are of full age, treating upon equal terms without imposition, and there is an inequality, even if it is a gross one, the Court in general has not set it aside.[6]

In Heathcote v. Paignon[7] the same Lord Chancellor drew a distinction between mere inadequacy of consideration, which is insufficient as a ground for setting aside a transaction, and the evidence which arose from such inadequacy.

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1 (1828) 1 Mol. 328.

2 Ibid., 335. See also Note, (1935) 35 Col.L.Rev. 1090.

3 (1778) 1 Bro. C.C.1.

4 Ibid., 6.

5 Ibid., 9.

6 Ibid.

7 (1787) 2 Bro. C.C. 167.

> If there is such inadequacy as to show that the person did not understand the bargain he made, or was so oppressed that he was glad to make it, knowing its inadequacy, it will shew a command over him which may amount to fraud. If the transaction be such as marks overreaching on one side, and imbecility on the other, it puts the parties in such a situation, as to shew that it could not have taken place without superior powers on the one side over the other.[1]

In Griffith v. Spratley,[2] Eyre L.C.B. agreed with the principle set out in Heathcote v. Paignon but again reiterated the view that inadequacy of consideration would not be a good enough reason for relieving a person who had wittingly and willingly entered into the agreement. But

> /W/hen you see distress on the one side and money on the other, and a wish on the one side to press that distress into a submission to his own terms, inadequacy of price goes a great way in warranting the court to infer from this, that some sort of fraud was used to draw the other party into the bargain.[3]

The foregoing cases generally stress that fraud will only be presumed where the parties are unequal and the consideration is grossly inadequate. However, in Gibson v. Jeyes[4] Lord Eldon L.C. drew a distinction between the situation where the inadequacy is so great that by itself it is evidence of fraud and lesser inadequacy which will constitute fraud only in conjunction with inequality in the positions of the parties. Whether inadequacy is by itself sufficient reason for setting aside the agreement will depend upon

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1 Ibid., 175.

2 (1787) 1 Cox 383.

3 Ibid., 389.

4 (1801) 6 Ves. 266.

whether it is "so gross as to shock the conscience of any man, who heard the terms."[1] Lord Eldon followed up this new departure by maintaining in an obiter dictum in Coles v. Trecothick that inadequacy of consideration can be so gross as to amount "in itself to conclusive and decisive evidence of fraud."[2]

Courts have, in subsequent cases, made obiter statements to the effect that while "mere" undervalue was only evidence of fraud and required "additional circumstances" before fraud would have been proven, gross undervalue was conclusive proof of fraud.[3]

It is perhaps significant that these utterances remained merely obiter and that in the more modern cases there is no trace of a similar principle. Apart from the fact that such a principle would have been difficult to defend within a system of freedom of contract, the absence of any ratio decidendi supporting it showed that in the vast majority of cases where gross inadequacy of consideration was to be found there were also additional impeaching factors present which took the cases outside the narrow confines of that principle. It is difficult to think of cases where, in contracts for consideration, a person would conclude a grossly unfair contract which could not, in part at least, be explained by some bargaining handicap such as necessity, distress or weakness.

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1 Ibid., 273.

2 (1804) 9 Ves. 234, 246.

3 Stilwell v. Wilkins (1821) Jac. 280, 282; Summers v. Griffiths (1866) 35 Beav. 27, 33; Clark v. Malpas (1862) 4 De G., F. & J. 401, 403; Butler v. Miller (1867) I.R. 1 Eq. 195, 211; Davies v. Cooper, (1840) 5 My. & Cr. 270, 277.

The cases surveyed are, however, important in the way they highlight the importance of inadequacy of consideration within the equitable doctrine of fraud.

(ii) Catching Bargains with Expectant Heirs[1]

The jurisdiction against catching bargains with expectant heirs was the oldest of the branches of equitable fraud. It first came to be applied extensively in the late seventeenth century, but there are indications that it went back to the Court of Star Chamber[2] and was ultimately derived from the Senatus Consultum Macedonianum. The aim of the latter was to prevent spendthrifty children "loaded with debts for borrowed moneys, which they used in extravagance, /from plotting/ against their parents' lives."[3]

The scope of this jurisdiction, both as regards the category of "expectant heir" and the type of agreement involved, eventually came to be very wide. It comprised sales, charges, leases and mortgages of reversions, remainders or of "any future interest, vested or contingent, in real or personal property, and /included/ a bare hope to inherit or receive some benefit."[4] Equity's scrutiny

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1 See generally, J.P. Dawson, Economic Duress - An Essay in Perspective (1947) 45 Mich.L.Rev. 253, 267-276. Also the thorough survey of the relevant material in Sheridan, Fraud in Equity, 132-145.

2 Earl of Chesterfield v. Janssen (1751) 2 Ves. 125, 139; Davis v. Duke of Marlborough (1819) 2 Swan. 108, 170 per Lord Eldon L.C.

3 Justinian, Institutes, IV, 7.7. as cited by Bellot, op. cit. 110

4 Sheridan, op. cit., 134. See, for example, Nott v. Hill (1683) 1 Ver. 167 - Transfer of a remainder in tail worth £800 in return for £30 cash and £20 annuity set aside; Twisleton v. Griffith (1716) 1 P.Wms. 310 - Transfer set aside of a remainder in tail worth £150 p.a. in return for only £1050 given by defendant, although plaintiff's father who held the life estate was old and sickly and died within two years of the conclusion of the agreement;

also extended to post-obit bonds[1] by which a person who was lent a sum of money undertook to repay a larger amount, usually double the amount of the loan, but frequently much more, if he survived a specified person from whom he stood to inherit. Instances of judicial intervention pre-dating even those cases were provided by sales of goods[2] and the granting of annuities[3] or rent-charges[4]

Baugh v. Price (1752) 1 Wils. K.B. 320 - Court set aside an agreement by plaintiff to convey an estate in fee simple worth £3,000 but subject to the estate for his father's life, for £1,500 and a house worth £200; Crowe v. Ballard (1790) 1 Ves. 215 - A legacy of a £1,000 payable on the death of a lady aged sixty-nine sold for £310. Court set aside the sale; Evans v. Peacock (1809) 16 Ves. 512 - Plaintiff agreed to convey within a month of the death of his father several estates, the value of which was calculated as being between £700 and £2040, in consideration of £500 paid to him. The court set aside the transaction.

1 The courts regularly set aside post-obit bonds, decreeing that the plaintiff should be liable only for the amount actually advanced plus interest. Contra: Batty v. Lloyd (1682) 1 Ver. 141; Barny v. Beak (1682) 2 Ch.Ca.136. See, however, the following cases where relief was given: Barney v. Tyson (1684) 2 Vent. 359; Berney v. Pitt (1686)2 Ver. 14 - Plaintiff borrowed £2,000 and agreed to pay £5,000 if he survived his father, else nothing; Wiseman v. Beak (1690)2 Ver. 121; Curwyn v. Milner (1731) 3 P. Wms. 292 n. - £500 lent on condition that £1,000 be repaid; Osmond v. Fitzroy (1731) 3 P.Wms 129; Evans v. Chesshire (1803) Ves. Sen. Supp.300 - £300 borrowed on condition that £600 be repaid; Marsack v. Reeves (1821) 6 Madd. 108.

2 Waller v. Dalt (1676) 1 Ch.Ca.276; Draper v. Dean (1679) Rep.t.F. 439; Berney v. Fairclough (1680)2 Swan. 139n.; Bill v. Price (1687) 1 Ver. 467; Lamplugh v. Smith (1688) 2 Ver. 77; Witley v. Price (1688) 2 Ver. 78; Freeman v. Bishop (1740) Barn C. 15; See also Barker v. Vansommer (1782) 1 Bro.C.C. 149, 151 where Lord Thurlow L.C. stated that if the transaction was an ordinary sale of goods, the court would not intervene, but as it was "an advancement of goods, instead of money, to supply /the buyer's/ necessities" the buyer-plaintiff is liable only for the amount that he eventually obtained by reselling the goods.

3 See Henley v. Axe (1786) 2 Bro.C.C. 17 in which Lord Chancellor Thurlow upheld the agreement. Also Pawlett v. Pleydell (1679) 79 Selden Society, 739.

4 Earl of Ardglasse v. Muschamp (1684) 1 Ver. 237; Gwynne v. Heaton (1778) 1 Bro.C.C. 1; Wardle v. Carter (1835) 7 Sim. 490.

involving expectant heirs, which merely served as cloaks for loans of money at exorbitant rates of return. This again indicates the extent to which the jurisdiction against unfair contracts was formed and developed by analogy to the usury laws.

Initially this doctrine of relief had a limited objective, the protection of the landowning class against its own prodigality and dissipation. The expectant heir who needed cash urgently was, because of his inability to provide security for a loan and the uncertainty of his financial prospects, precluded from obtaining money at a reasonable rate of interest. He was thus thrown back onto frequently unscrupulous money-lenders who were only too eager to fulfil his immediate needs. The cost of raising money from these sources was generally extremely high and the caselaw paints a vivid picture of desperate heirs who, in an attempt to finance past or future extravagances, had ensnared themselves in this way. The Court of Chancery was not prepared to countenance this state of affairs and when the judges were called upon to adjudicate in the confrontation between expectant heirs and their supposed benefactors, they came out unequivocally on the side of the former. Their motive in taking this stance was to discourage prodigality and to prevent the ruin of "ancient families" as a result of the dispersion of their property and wealth which would inevitably have followed from holding the expectant heirs bound by their greatly disadvantageous agreements.[1] The rule which thus arose in respect of

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[1] See the statement by Lord Chancellor Talbot in Cole v. Gibbons (1734) 3 P.Wms. 290, 293; see also Earl of Portmore v. Taylor (1831) 4 Sim. 182, 213.

transactions with expectant heirs dealing in anticipation of their expectancies, was clear: they would be set aside or modified unless they were substantively fair, that is unless they involved no great disparity between the values exchanged. The possibility, alluded to by counsel for the defendant in a number of cases, that courts could, by too strict an insistence on the standard of equivalence, deprive the necessitous heir of his last remaining source of financial relief, left the courts undeterred.[1]

Although the wisdom of an objective so narrow and so peculiarly related to a particular social class was not questioned at the time,[2] the need for a wider principle was clearly felt. A ready vehicle by means of which such an extension could be effected was provided by the economic necessity and weakness with which the heir who entered into these transactions was generally afflicted. And as soon as the necessity of the heir came to be regarded as a crucial element in the formula on which relief was based, the earlier notion that the doctrine pertained to young heirs only, fell out of favour.[3] A small number of cases during the latter part of the seventeenth century and the first half of the eighteenth century referred, in addition to the economic necessity of the heir, to his

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1 Such a possibility was in fact welcomed by Lord Cowper L.C. in Twisleton v. Griffith (1716) 1 P.Wms. 310, 313.

2 Some doubts were expressed in a few later cases. See, for example, Shelly v. Nash (1818) Madd. 232, 236.

3 As early as Wiseman v. Beak (1690) 2 Ver. 121 relief was granted to an heir who was nearly 40 years old and described by counsel for the defendant as a man of the world. Although the majority of plaintiffs in these cases were young that was not a sine qua non for relief.

inexperience or ignorance as factors underlying the doctrine of relief.[1]

Despite an insistence by Lord Nottingham on a showing of sharp practice on the part of the defendant as a prerequisite for relief[2] this requirement soon disappeared. Lord Jeffreys who succeeded Lord Nottingham as Chancellor showed himself to be far more favourably disposed towards giving relief than his predecessor. Harbouring a strong bias in favour of the noble families of the time he proceeded to give relief wherever the expectant heir could show that the contract was unfair. This attitude was followed by the Lords Commissioners who succeed Lord Jeffreys and was to remain the approach followed by the Chancery courts until Lord Hardwicke's exposition of the law in Earl of Chesterfield v. Janssen.[3]

The test which had been developed by the Chancery courts and applied in the vast majority of cases was objective: relief was dependant only upon a finding that one of the parties to the agreement was a necessitous and destitute heir contracting in anticipation of his expectancy, and that the heir would receive an inadequate consideration in return for his own performance.[4] Such

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1 In Herne v. Meeres (1687) 1 Ver. 465 it seems as if considerations of actual fraud also tainted the bargain. See also Osmond v. Fitzroy (1731) 3 P.Wms. 129 - breach of trust; Gould v. Okeden (1731) 4 Bro. P.C.198; Cole v. Gibbons (1734) 3 P.Wms.290.

2 See, for example, Pawlett v. Pleydell (1679)79 Selden Society 739.

3 (1751) 2 Ves. 125.

4 In Gwynne v. Heaton (1778) 1 Bro.C.C.1, 10, Lord Thurlow L.C. commented on Curwyn v. Milner (1731) 3 P.Wms. 292n. saying that it was a case perfectly free from fraud. And in Berney v. Pitt (1686) 2 Ver. 14, 15-16 Jeffreys L.C. said that although there was no evidence "of any practice used by the defendant ... to draw the plaintiff into this security; yet in respect merely to the unconscionableness of the bargain" relief should be granted.

an objective approach was in full accord with the policy of the courts, the aim of which was not to ensure that consent to an unfair contract should be unimpeachable, but rather to discourage and if possible to prevent inequitable agreements with a certain class of contracting party altogether. By doing so the courts clearly recognised the reality of the situation, which was that in most cases the heir entered into a grossly unequal bargain, not because he was unaware or ignorant of the effect of his actions, but because he was compelled to do so by his dire financial circumstances. To such an objective approach considerations of usury, although formally excluded by the contingency on which the heir's counterperformance usually depended, were obviously of greater relevance than fraud with its emphasis on the propriety of consent.[1] The appositeness to the present doctrine of the principles of usury becomes even clearer when viewed against the background of the general unwillingness of the courts to take into account the risk which was involved to the defendant who, in almost every case, stood to lose his entire return if the contingency on which repayment depended - usually the expectant heir outliving the testator - was not realized.[2] That the transactions were often extremely hazardous to the defendant was seldom taken into account. Where the risk was considered it was

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1 This was especially true of the cases dealing with attempts to raise money by purchases of goods with the view of reselling them. See the cases cited on page 79, note 2.

2 In a few exceptional cases the risk was taken into account. See Barny v. Beak (1682) 2 Ch.Ca. 136; Hobson v. Trevor (1723) 2 P.Wms. 191; Nichols v. Gould (1752) 2 Ves. 422. But in Benyon v. Fitch (1866)35 Beav. 570, the risk involved was expressly disregarded.

generally only to show that by insuring the life of the expectant all risk had been excluded.[1] With the most important distinction between these transactions with heirs and usurious moneylending transactions generally disregarded by the courts it was logical that ideas should filter through from the doctrine of usury.

A comprehensive restatement in terms of fraud came in the leading case of Earl of Chesterfield v. Janssen, a case involving a post-obit bond, where Lord Hardwicke L.C. discussed these "catching bargains with heirs, reversioners, or expectants, in the life of the father ..., against which relief always extended."[2] According to his Lordship that jurisdiction was based on fraud which was always inferred from "the circumstances or conditions of the parties contracting: weakness on one side, usury on the other, or advantage taken of that weakness."[3] It is thus clear that despite postulating fraud, albeit equitable fraud, as the basis of relief the doctrine had not changed substantively. That it was felt necessary at that time to describe the basis of intervention as fraud does, however, shows the increasing sensitivity in Chancery towards the growing importance of consensus in the concept of contract.

As Lord Hardwicke indicated, fraud would be presumed from the fact that the plaintiff, when he concluded the contract, had been suffering from a bargaining handicap, coupled with the fact that

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1 See for example Evans v. Chesshire (1803) Ves. Sen. Supp. 300; Evans v. Peacock (1809) 16 Ves. 512.

2 (1751) 2 Ves. 125, 157.

3 Ibid.

the transaction was in itself unfair. The unfairness of the contract was generally sufficient to show that the plaintiff's weakness had been taken advantage of by the defendant.[1] This presumption was, however, rebuttable - the defendant could still show that the plaintiff, although weak, had assented to the contract freely and while understanding the level of exchange involved. This was, of course, an unlikely event and in most cases where an heir had agreed to a highly disadvantageous bargain it was simply accepted that he had been taken advantage of.[2]

While it was the economic necessity of the heir which rendered him vulnerable and thus worthy of judicial protection it happened quite often that there was no thorough investigation of the heir's economic circumstances. If the bargain was disadvantageous and the plaintiff an expectant heir it was often assumed that he must have been in economic difficulty. Where additional evidence

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1 The following statement by Sir John Leach V.C. in Marsack v. Reeves (1821) 6 Madd. 108, 109 showed clearly that "taking advantage of a necessitous heir" meant no more than that the defendant had given inadequate consideration: "It has long been a settled principle of Courts of Equity that those who deal with persons who have no present property, and only expectations from persons living, possess so much advantage over those with whom they deal that this Court will not permit a party so dealing to recover, unless he has given the actual value of the thing which he has purchased."

2 See the dictum by Lord Eldon L.C. in Underhill v. Horwood (1804) 10 Ves. 209, 219 that "... if the terms are so extremely inadequate as to satisfy the conscience of the Court by the amount of the inadequacy, that there must have been imposition, or that species of pressure upon distress, which in the view of this Court amounts to oppression..." then relief would be granted.

showing that the heir was liable to be imposed upon, such as recklessness, improvidence, or unsteadiness, (often caused by heavy drinking), was present that was, of course, seized upon by the courts as proof, in conjunction with the disparity in the values exchanged, that the heir had indeed been the victim of fraud. But such evidence merely strengthened the finding of the court and was by no means necessary for it. In Ryle v. Swindells, for example, the court reinforced its decision that a sale at an undervalue should be set aside, by stating that

> /T/he general condition of this man, which is represented to have been that of extreme indigence, ignorance, imbecility of intellect, and habitual inebriety was such as should render him an object of the protection of the Court. I think that no man capable of dealing for his own interests, could have acceded to that stipulation.[1]

Furthermore the fact that it was often the plaintiff/heir who had been hawking around his expectancy and who had stipulated the terms of the agreement was either regarded as of no consequence or as indicative only of the economic necessity of the heir.[2]

The objective approach followed by the courts was also not disproved by those decisions which refused to set aside a subsequent agreement confirming the first. In Cole v. Gibbons,[3] Lord Chancellor Talbot denied relief from the sale of a contingent legacy, because it was confirmed by the heir after the legacy had become due. His Lordship stated that if everything had depended upon the first

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1 (1824) M'Cl.519, 526.

2 See, for example, Evans v. Peacock (1809) 16 Ves. 512; Bowes v. Heaps (1814) 3 V.& B. 117, 119 where Sir William Grant M.R. said: "It is not every bargain which necessity may induce one man to offer that another is at liberty to accept."

3 (1734) 3 P.Wms. 290.

assignment he would have set it aside "as being an unreasonable advantage made of a necessitous man; but seeing the /plaintiff/ was afterwards fully apprised of every thing ... and since not the least fraud or surprize had appeared on the part of the defendant"[1] the court could not intervene. As the bargaining handicap attaching to the plaintiff at the time of the assignment had, as a result of the legacy subsequently having become due, been removed by the time of the confirmation, fraud could not be presumed any more.

The position at the end of the eighteenth century can be summarised by saying that relief was given to an expectant heir who, in anticipation of his expectancy, had concluded an unfair contract in respect of his expectancy. This situation continued well into the nineteenth century.[2] Protection had to some extent become an incident of status. Sir George Jessel M.R. reflected the true practice of the courts when he said:

> The point to be considered is, was this a hard bargain? The doctrine has nothing to do with fraud ... It has been laid down in case after case that the Court, wherever there is a dealing of this kind, looks at the reasonableness of the bargain, and if it is what is called a hard bargain, sets it aside.[3]

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1 Ibid., 294. The same effect was given to a subsequent confirmation in Earl of Chesterfield v. Janssen (1751) 2 Ves. 125, but in Baugh v. Price (1752) 1 Wils. K.B.320, Baron Smythe refused to give effect to a confirmation on the ground that the heir was not fully apprised of the facts when he made the confirmation.

2 See Newton v. Hunt (1832) 5 Sim.511 where an agreement was set aside despite the fact that throughout the negotiations the plaintiff had the advice and assistance of an experienced solicitor; Davies v. Cooper (1840) 5 My. & Cr. 270; Edwards v. Burt (1852) 2 De G.M. & G. 55; St. Albyn v. Harding (1859) 27 Beav.11; Bromley v. Smith (1859) 26 Beav. 644.

3 Benyon v. Cook (1875) L.R.10 Ch.App. 389, 391.

The nineteenth century brought about significant changes in relation to the determination of the fairness or adequacy of consideration. At an early stage a practice developed to transfer the burden of proving substantive fairness on to the defendant.[1] This procedural handicap could in itself be extremely hazardous to the defendant. As the adequacy of consideration could not, in theory at least, be determined with the benefit of hindsight, but depended upon circumstances prevailing at the time of the conclusion of the contract the defendant could be prevented from discharging the burden of proof merely because the lapse of time between the conclusion of the transaction and the bringing of the action for relief had led to a loss of relevant evidence.[2] The defendant's predicament was also worsened by the fact, frequently acknowledged by the courts, but seldom employed in the defendant's favour, that it was often extremely difficult to determine the value of a contingent future interest. In the main, the courts, in accordance with their view that the expectant heir was particularly deserving of judicial protection, preferred to err in his favour.

The courts' determination to protect their charge was also evident from their strict application of the requirement of adequacy of consideration. In Underhill v. Horwood[3] Lord Eldon L.C. required that the "real" value of the annuity should have been given.

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1 Gowland v. De Faria (1810) 17 Ves. 20.

2 See, for example, Salter v. Bradshaw (1858) 26 Beav. 161.

3 (1804) 10 Ves. 209.

This was something different from the market value: "/T/he market price may be under the value."[1] And in Gowland v. De Faria[2], Sir William Grant M.R. maintained that the defendant had to show that "full" value, which was interpreted as the actuarial value, had been given.[3] The only situation where the actuarial value-standard was not adhered to was where the reversionary interest was bought at a public auction.[4]

It was suggested by Lord Brougham L.C. in King v. Hamlet[5] that

> the extraordinary protection given in the general case must be withdrawn, if it shall appear that the transaction was known to the father or other person standing in loco parentis.

However that notion was frequently attacked in later cases and in Talbot v. Staniforth[6] the Vice-Chancellor said that it only meant that where the heir acted with the best protection and advice available he might be presumed to have got a fair market price, but that no further inference would be drawn from that fact.

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1 Ibid., 220.

2 (1810) 17 Ves. 20.

3 See also Ryle v. Swindells (1824) M'Cl. 519; Hincksman v. Smith (1827) 3 Russ. 433.

4 Shelly v. Nash (1818) Madd. 232. In Fox v. Wright (1821) 6 Madd. 111, Sir John Leach V.C. held that a sale of post-obit bonds without reserve at an auction did not necessarily fall within the rule in Shelly v. Nash as it should have been clear that the heir was in distress and needed money so much that he undertook with the bidders not to take such precautions by which every provident seller at an auction protects himself against an inadequate price.

5 (1834) 2 My. & K. 456, 474.

6 (1861) 1 J. & H. 484.

This extremely strict attitude held sway for a while until it became evident to the courts that a value which was unrealizeable in practice was unacceptable as a standard of adequate consideration, and as a result, a shift occurred in favour of the market price.[1] Where the market price was difficult to establish the courts accepted two-thirds of the actuarial value as an acceptable yardstick.[2]

At the same time that the standard of adequacy was relaxed a tendency grew up to require the most rigorous adherence to that yardstick, and especially during the late 1850s and 1860s the most slender difference between the market value and the amount actually advanced to the expectant heir was a sufficient cause to set aside the transaction. The defendant had to show that he gave the "just" value, or paid a "fair, sufficient and full price" - giving "substantial value" was not enough.[3]

Such over-enthusiasm by the courts eventually moved the legislature to pass the Sales of Reversions Act 1867, which in section 1 provided that

> No purchase, made bona fide and without Fraud or unfair Dealing, of any Reversionary Interest in Real or Personal Estate shall hereafter be opened or set aside merely on the Ground of Undervalue.[4]

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1 Headon v. Rosher (1825)M'Cl. & Yo. 89; Potts v. Curtis (1832) Yo. 543; Earl of Aldborough v. Trye (1840) 7 C.& F. 436.

2 Potts v. Curtis (1832) Yo. 543.

3 In Edwards v. Browne (1845) 2 Coll. 100, the sale of a reversionary interest worth between £1,950 and £2,800, but sold for £1,700 was set aside; Foster v. Roberts (1861) 29 Beav. 467 - The bona fide purchase of a reversionary interest worth £400 for £370 set aside; Jones v. Ricketts (1862) 31 Beav. 130 - A purchase of a reversionary interest for £200 was set aside on the sole ground that the purchaser had paid £38 less than its real value.

4 The Sales of Reversions Act, 1867, has been replaced by the Law of Property Act 1925, section 174.

This provision not only had a limited scope,[1] but it was also, consistent with its language, very narrowly construed to pertain only to those transactions where undervalue was the only ground of relief.[2] The Act could thus not prevent the giving of relief where "necessity" or "oppression" etc. was hauled in as an additional ground.

In Earl of Aylesford v. Morris,[3] Lord Selborne L.C. in an obiter dictum reviewed the effect of that Act and the abolition of the usury laws upon the jurisdiction relating to transactions with heirs. His Lordship said:

> The usury laws proved to be an inconvenient fetter upon the liberty of commercial transactions; and the arbitrary rule of equity as to sales of reversions was an impediment to fair and reasonable, as well as to unconscionable, bargains. Both have been abolished by the Legislature; but the abolition of the usury laws still leaves the nature of the bargain capable of being a note of fraud in the estimation of this Court; and the Act as to sales of reversions ... is carefully limited to purchases made bona fide and without fraud or unfair dealing, and leaves under-value still a material element in cases in which it is not the sole equitable ground for relief. These changes in the law have in no degree whatever altered the onus probandi in those cases, which, according to the language of Lord Hardwicke, raise 'from the circumstances or conditions of the parties contracting - weakness on one side, usury on the other, or extortion, or advantage taken of that weakness' - a presumption of fraud. Fraud does not here mean deceit or circumvention; it means an unconscientious use of the power arising out of these circumstances and conditions; and when the relative position of the parties is such as prima facie to raise this presumption, the transaction cannot stand unless the person claiming the benefit of it is able to repel the presumption by contrary evidence, proving it in point of fact fair, just, and reasonable.[4]

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1 As the Act referred only to reversionary interests some transactions which also fell within the scope of this jurisdiction, such as those relating to post-obit bonds, were not affected.

2 See Miller v. Cook (1870) L.R. 10 Eq.641; Tyler v. Yates (1871) L.R.Ch.App. 665; In re Slater's Trusts (1879) 11 Ch.D.227.

3 (1873) L.R. 8 Ch.App. 484.

4 Ibid., 490-491.

Lord Selborne's reasoning was accepted in some later cases[1] but the question whether inadequacy of consideration could per se be proof of unfair dealing continued to plague the courts. In O'Rorke v. Bolingbroke[2] the majority of the House of Lords declined to intervene in the transaction despite the undervalue because there was no fraud and the agreement was made in good faith. On the other hand, in Brenchley v. Higgins[3] it was suggested in an obiter dictum that undervalue alone may amount to evidence of unfair dealing so as to take a cause out of the limitation imposed by the Sales of Reversions Act.

Where it was the expectant heir who came to the Chancery Courts for relief and the court decided that it was a proper case for intervention the transaction was generally set aside and the heir made liable only for the amount which he had actually received plus interest at a rate determined by the court. In a small number of cases, however, it was not the heir, but his counterparty who came to court claiming specific performance of the agreement and in such a case the courts could, of course, refuse this by employing the usual tests of fairness required for specific performance.[4]

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1 Benyon v. Cook (1875) L.R. 10 Ch.App. 389, 392; O'Rorke v. Bolingbroke (1877) 2 App.Cas. 814.

2 (1877) 2 App.Cas. 814.

3 (1900) 12 Digest 140.

4 See for example Beckley v. Newland (1723) 2 P.Wms. 182; Harwood v. Tooke (1812) 2 Sim. 192; Hobson v. Trevor (1723) 2 P.Wms. 191.

(iii) Taking Advantage of Weakness and Necessity[1]

The jurisdiction against catching bargains with expectant heirs was the oldest of the various branches of equitable fraud. Co-existing and closely intertwined with it was another kind of fraud which according to Lord Hardwicke

> may be presumed from the circumstances and condition of the parties contracting ... /I/t is wisely established in this court to prevent taking surreptitious advantage of the weakness and necessity of another: which knowingly to do is equally against the conscience as to take advantage of his ignorance: a person is equally unable to judge for himself in one as the other.[2]

In the later case of Nevill v. Snelling,[3] Denman J., in setting aside on equitable terms certain moneylending transactions which stipulated for an exorbitant rate of interest, characterised the jurisdiction as follows:

> The real question in every case seems to me to be the same as that which arose in the case of the expectant heirs and reversioners before the special doctrine in their favour was established - that is to say, whether the dealings have been fair, and whether undue advantage has been taken by the money lender of the weakness or necessities of the person raising the money. Sometimes extreme old age has been taken advantage of, and the transaction set aside. Sometimes great distress. Sometimes infancy has been imposed upon, and transactions, though ratified at the full age, have been set aside because of the original vice with which they were tainted. In every case the Court has to look at all the circumstances. In some cases may result the conclusion that there exists mere inadequacy of price, or exorbitance of interest charged, in which case the transaction will not be interfered with. But in others taking the whole history together, it may present so many features of unconscientiousness, extortion, and unfair dealing on the

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1 See generally, Sheridan, Fraud in Equity, 73-86.

2 Earl of Chesterfield v. Janssen (1751) 2 Ves. 125, 155-156.

3 (1880) 15 Ch.D. 679.

> one side and weakness on the other, as to compel the Court to exercise its equitable jurisdiction, at all events so far as to restrain the profits of the money lender within fair and reasonable bounds.[1]

The types of transaction to which this branch of equitable fraud has been applied are numerous and include sales and purchases of land or interests in land,[2] of shares in sailors' prizemoney[3], of shares in estates,[4] moneylending transactions,[5] lease agreements,[6] a conveyance of interests in premises,[7] mortgage agreements,[8] assignations,[9] and voluntary settlements and conveyances.[10] The courts have been particularly strict where the latter type of transactions have been involved and in Phillips v. Mullings[11] it was intimated that a voluntary settlement will be set aside unless it can be shown that all its provisions are proper and usual, and if there are unusual provisions, that they were brought to the notice of and understood by the settlor.

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1 Ibid., 702-703.

2 Slator v. Nolan (1876) I.R.11 Eq. 367; Butler v. Miller (1867) I.R. 1 Eq.195; Baker v. Monk (1864) 4 De G.J. & S. 388.

3 How v. Weldon & Edwards (1754) 2 Ves. 516; Baldwin & Alder v. Rochford (1748) 1 Wils. K.B. 229.

4 Sturge v. Sturge (1849) 12 Beav. 229; Wood v. Abrey (1818) 3 Madd.417.

5 Nevill v. Snelling (1880) 15 Ch.D.679; Stanhope v. Cope (1741) 2 Atk. 231; Rich v. Sydenham (1671) 1 Ch.Ca. 202.

6 Willan v. Willan (1814) 2 Dow 274.

7 Creswell v. Potter [1978] 1 W.L.R. 255; Backhouse v. Backhouse [1978] 1 W.L.R. 243.

8 Ford v. Olden (1867) 3 L.R. Eq. 461; Cockell v. Taylor (1852) 15 Beav. 103.

9 Maskeen v. Cole (1733) 2 Madd. 42ln. - assignation of conditional legacy; M'Diarmid v. M'Diarmid (1828) 3 Bli.N.S.374; Selby v. Jackson (1844) 6 Beav. 192.

10 Blachford v. Christian (1829) 1 Kn.73; Grealish v. Murphy (1946) I.R. 35; Forshaw v. Welsby (1860) 30 Beav. 243.

11 (1871) 7 L.R.Ch.App. 244.

The relation between the two main branches of equity's jurisdiction against fraud, the doctrine against catching bargains with heirs and that against taking unfair advantage of weakness and necessity, was a close one, and although it cannot be said that the latter developed solely out of the former, it is nevertheless true that the insights which were gained from the jurisdiction against catching bargains with heirs were instrumental in the rapid development of the latter. It has been noted before that although the protection of heirs arose initially because of narrow class-based objectives the fact that a contracting heir often suffered from mental or physical disability or was commercially inexperienced, poor or under economic pressure soon came to be regarded as equally compelling reasons why the courts should intervene to give such parties relief from disadvantageous contracts. This enlarged perspective had a profound effect on equity's jurisdiction; not only was the protected class of expectant heir widened as a result, but the courts also began to relieve where no heir was involved and where the only impeaching factor apart from the unfairness of the transaction, lay in the inequality between the parties. Initially the causes of inequality of which the courts took note was of the more obvious kind, like mental weakness or disease. But as the courts became more confident about the propriety of intervening on the basis of inequality between the parties, the variety of causes of inequality of which cognisance was taken increased and came to include such factors as social and economic deprivation.

In order to constitute fraud in the sense in which the term

is used here it was necessary to show firstly, that at the time of the conclusion of the contract the disadvantaged party was suffering from a specific bargaining handicap which rendered him particularly vulnerable to imposition by the defendant and secondly, that this inequality between the parties had in fact been taken advantage of by the defendant. A host of terms other than "taking advantage of" was used by the courts to convey the same meaning, for example "oppress", "exploit", "coerce", "contrive" or "overreach". Just as was the case under equity's jurisdiction against catching bargains with heirs the requirement that advantage had been taken of the plaintiff's handicap was here inferred from the unfairness of the transaction: where a party who, because of his particular handicap, was liable to be taken advantage of concluded an unfair contract with a stronger party, the unfairness was generally sufficient to show that he had in fact been taken advantage of. The function of the terms such as "imposition" was merely to provide a causal link between the disadvantage attaching to the plaintiff and the unfairness of the contract. The law has been reluctant to set aside contracts solely because of inadequacy of consideration and at the same time bargaining handicaps such as those that were regarded as relevant in this jurisdiction were never recognised to be in themselves a cause for giving relief from a transaction. It was therefore necessary to combine these two factors so as to form a ground for relief which did not rest solely on the one or the other.

It was not necessary that the disadvantage or bargaining handicap of the weaker party be caused or aggravated by the stronger.

Where, however, the latter did ensnare the weaker, the courts were all the more ready to grant relief.[1] Although it has seldom been positively stated that the exploiter had to be aware of the plaintiff's weakness[2] and had to appreciate that the contract was unfair, these facts were usually assumed by the courts and the better view would be that they were indeed necessary prerequisites for relief. The cases in which it was said that relief would be given even if the stronger party was ignorant of the weaker person's disadvantage and of the unfairness, were few.[3]

Not only did the courts infer fraud from only the inequality between the parties plus the unfairness of the bargain, but in the nineteenth century the tendency developed to place on the stronger party the burden, once the other had proved his bargaining handicap, to show that the transaction was fair.[4]

As I have indicated equitable fraud here meant that advantage had been taken of an inequality between the parties to the contract. In order to establish the scope of the doctrine it is thus necessary to determine which characteristics or factors could, in the view of the courts, indicate that such an inequality existed.

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1 Nevill v. Snelling (1880) 15 Ch.D. 679, 696 and the cases there cited.

2 Except in those cases where an unfair contract had been concluded with a person who suffered from mental impairment. See post p.99.

3 See the obiter dictum by Sargent L.J. in York Glass Co.Ltd. v. Jubb (1925) 134 L.T. 36, 43.

4 Baker v. Monk (1864) 4 De G. J. & S. 388, 391; Creswell v. Potter /1978/1 W.L.R. 255; Longmate v. Ledger (1860) 2 Giff. 157.

It is neither possible nor desirable to give an exhaustive list of the types of weakness which, if taken advantage of, would lead to a finding of fraud. The question whether a party merited judicial protection depended upon the disparity of bargaining strength between the parties rather than upon the specific weakness of one party. In Slater v. Nolan the Master of the Rolls expressed the idea as follows:

> I take the law of the Court to be that if two persons - no matter whether a confidential relation exists between them or not - stand in such a relation to each other that one can take an undue advantage of the other, whether by reason of distress or recklessness or wildness or want of care, and where the facts show that one party has taken undue advantage of the other, by reason of the circumstances I have mentioned - a transaction resting upon such unconscionable dealing will not be allowed to stand: and there are several cases which show, even where no confidential relation exists, that, where parties are not on equal terms, the party who gets a benefit cannot hold it without proving that everything has been right and fair and reasonable on his part.[1]

The following classification of factors which the courts have recognised as leading to inequality between the parties is thus arbitrary and made solely to facilitate the subsequent discussion. The factors which cause an impairment of bargaining power can be broadly divided into three groups: firstly, a weakening of the body and/or the mind. Included are mental impairment, intoxication, illness or old age; secondly, the inferior social position or status of a party. Within this category fall poor, illiterate and uneducated people, the young, and generally those who are underprivileged; thirdly, economic necessity and distress. These three

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[1] (1876) I.R.11 Eq. 367, 386-387.

categories are not exclusive of each other and frequently a variety of factors from the different categories concur in one party.

(iiia) Impaired Bargaining Power arising from a Weakening of Body and Mind

1. Mental Weakness

At common law the mental disorder of a contracting party had no effect on the validity of an agreement unless the party could show that because of his mental incompetence he did not understand what he was doing and also that the other party to the agreement was aware of his disorder.[1] Mere mental weakness did not affect the validity of an agreement. Equity on the other hand, gave relief from an unfair contract on the ground of equitable fraud if one party suffered from an enfeeblement of the mind even though it may not have affected his legal capacity, and if such weakness had been taken advantage of[2]. In Harrod v. Harrod, Page Wood V.C. declared that "if there be no unsoundness but mere dullness of mind, the question becomes entirely one of fraud."[3] The Chancery courts did not, for the purposes of establishing fraud, distinguish between various degrees of mental weakness.[4]

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1 Imperial Loan Co. Ltd., v. Stone (1892) 1 Q.B. 599. This refers only to mentally disordered people who are not "patients" in terms of the Mental Health Act 1959. As to the validity at common law of contracts concluded by mentally disordered people see also Chitty on Contracts, sections 535-541; W.G.H.Cook, Mental Deficiency and the English Law of Contract (1921) 21 Col.L.Rev.424; M.Brown, Can the Insane Contract? (1933) 11 Can.Bar Rev. 600.

2 Sheridan, op. cit., 75-78; Browne v. Joddrell (1827) M. & M. 105, 106; Dane v. Viscountess Kirkwall (1838) 8C.& P. 679.

3 (1854) 1 K. & J. 4, 7.

4 Sheridan, op. cit., 76.

It is a question of fact whether mental impairment exists in a particular case. The courts have seldom undertaken an exhaustive inquiry to determine whether mental weakness existed at the time that the contract was concluded. The evidence produced is often of an anecdotal nature or based on the subjective impressions of other persons[1] and proof of some eccentricities[2] on the part of the complainent will usually suffice to establish mental impairment.

Equity has not been, and is not, concerned with the contractual capacity of a party - it rather aims to protect a certain class of person who, because of the impairment of his mental faculties, is regarded as being particularly susceptible to imposition.[3] Alternatively, it is often stated that such a party is given protection because he is incapable of managing his affairs prudently.[4]

In order to constitute fraud it is necessary to show that the party suffering from mental impairment had been taken advantage of or had been imposed upon. This will usually be presumed if the contract is itself unfair and the defendant was aware of the plaintiff's weakness. M.D. Green has found that in American law -

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1 Gibson v. Jeyes (1801) 6 Ves. 266 - woman of old age whose mind had suffered as a result of the shock her health had received; Blachford v. Christian (1829) 1 Kn. 73 - aged 74 and in state of declining physical and mental state; Grealish v. Murphy [1946] I.R. 35.

2 Longmate v. Ledger (1860) 2 Giff. 157 - so strange and eccentric that any person who contracted with him would have to show that contract was fair; Bennet v. Vade (1742) 9 Mod.312 - believed that after amputation his toes would grow again.

3 See, for example, Stanhope v. Toppe (1720) 1 Bro.P.C.157, 164; Baxter v. Earl of Portsmouth (1826) 5 B. & C. 170, 172.

4 See, for example, Gibson v. Jeyes (1801) 6 Ves. 266, 273; Ball v. Mannin (1829) 3 Bli.N.S. 1, 12.

and a careful reading of the caselaw shows that the same is true of English law - the "abnormality" of the transaction in question is the major consideration upon which the courts proceed in deciding whether relief should be given from the transaction.[1] The presumption has been further loaded against the defendant by the tendency in some cases to throw on the latter the burden of establishing that "no unfair advantage had been taken of /the plaintiff's/ weakness and that he had paid a fair price."[2]

Inequality in the exchange is a relevant consideration not only to the question of whether the plaintiff was imposed upon or taken advantage of. It may also be of evidentiary value in deciding whether the plaintiff did in fact suffer from mental impairment. If the transaction was grossly unfair it can point to some mental weakness in the plaintiff.[3]

It would be expected from the requirement of imposition that a mentally impaired party would not be relieved from his contractual obligations if the defendant was unaware of the impairment and that was indeed the position adopted in a number of cases.[4] Yet, in York Glass Co. Ltd., v. Jubb, Sargent L.J. declared:

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1 M.D. Green, Proof of Mental Incompetency and the Unexpressed Major Premise (1944) 53 Yale L.J. 271.

2 Longmate v. Ledger (1860) 2 Giff. 157, 164. Also Selby v. Jackson (1844) 6 Beav. 192, 202.

3 See Green op. cit., 304-305.

4 Imperial Loan Co. Ltd. v. Stone (1892) 1 Q.B. 599, 601; Ball v. Mannin (1829) 3 Bli.N.S.1, 12; Selby v. Jackson (1844) 6 Beav. 192, 199.

> I have looked through a number of cases and I have not found a single case in which a contract has in fact been binding except where the contract was an ordinary reasonable contract.[1]

His Lordship maintained that his mind was

> entirely open on the question whether the fairness of the bargain is an essential element to the enforceability of the bargain against a person who was in fact a lunatic although not known to be such by the other contracting party.[2]

In the above quoted case of Harrod v. Harrod, Page Wood V.C., when referring to fraud arising from a contract concluded by a person dull in mind also, declared that "... it is a fraud to induce any person to enter into a contract which she does not understand."[3] This proposition seems correct. Generally a contract will only be allowed to stand if the party is capable of understanding the general purport of a contract when it is explained to him,[4] but this is a flexible standard and at times the courts have required a high degree of understanding. In Anderson v. Ellsworth[5] for example, the court set aside a voluntary deed in terms of which an old and mentally infirm lady conveyed all her property to the defendant. Despite her weakness she was found capable of transacting business. The deed and its effects were furthermore fully explained to her and she understood that she was donating all her belongings to the

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1 (1925) 134 L.T. 36, 43.

2 Ibid., 44.

3 (1854) 1 K. & J. 4, 7.

4 Gibbons v. Wright (1954) 91 C.L.R. 423, 483 per Dixon C.J.

5 (1861) 3 Giff. 154.

defendant. However, the court held that she did not appreciate the fact that she was immediately divesting herself of all her property and as this was highly improvident the transaction was set aside.

Mere non-understanding which cannot be traced to a disadvantage attaching to the party is not a sufficient ground for judicial intervention, but is ordinarily dealt with under mistake. Nevertheless, in Phillipson v. Kerry[1] a voluntary deed, executed by a person who was not of unsound mind, was set aside because she did not fully understand the nature and effect of the transaction.

2. Intoxication

A person who is in such an extreme state of intoxication that he is deprived of all reason has "no agreeing mind"[2] and is thus incapable of entering into a valid contract.[3] Drunkenness of a lesser degree does not affect the validity of an agreement at common law but may in equity lead to relief being given to the intoxicated person on the ground of fraud.

Even in equity, however, a state of intoxication is not by itself a sufficient ground either for setting aside an agreement or for refusing it specific performance.[4] This is especially true

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1 (1863) 32 Beav. 628.

2 Pitt v. Smith (1811) 3 Camp. 33, 34.

3 Cooke v. Clayworth (1811) 18 Ves. 12, 17.

4 Johnson v. Medlicott (1734) 3 P.Wms. 130n.; Cory v. Cory (1747) 1 Ves. 19; Cooke v. Clayworth (1811) 18 Ves. 12, 16; Blomley v. Ryan (1956) 99 C.L. R. 362, 403-405.

where the contract is a fair and reasonable one.[1] The courts have in fact been very careful not to create the impression that a person can escape his contractual obligations merely by claiming that he was drunk at the time of the conclusion of the contract. Where, however, the drunkenness was contrived by the counterparty[2] or the intoxicated person taken advantage of by leading him into an unfair contract, then he might be a proper object for relief in equity.

In the Australian case of Blomley v. Ryan[3] the court (McTiernan and Fullagar JJ., and Kitto J. dissenting) made a thorough survey of the law relating to the effect of intoxication on the validity of agreements. The question which the court had to answer was whether a sale, unfair in respect of the price, and one-sided and oppressive with regard to the general terms, made by an old, dissolute and habitually drunken person, could be set aside on these grounds. McTiernan J. held that these facts constituted equitable fraud,

> the essence of [which] is that advantage was taken of weakness, ignorance and other disabilities on the side of the respondent and the contract was derived from such behaviour and ... is an unfair bargain.[4]

And for the purposes of establishing equitable fraud no distinction was to be drawn between intoxication and any other disabilities by

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1 Cory v. Cory (1747) 1 Ves. 19.

2 See Say v. Barwick (1812) 1 V. & B. 195.

3 (1956) 99 C.L.R. 362.

4 Ibid., 385.

which parties may be affected: they all have the "common characteristic ... that they have the effect of placing one party at a serious disadvantage vis-à-vis the other"[1] Having thus established that the effect of drunkenness on the validity of agreements, rather than being a separate rubric, formed part of a wider jurisdiction in terms of which judicial protection is given to all parties suffering from impaired bargaining power, McTiernan J. expressed full accord with the statement by Lord Selborne L.C. that

> /W/hen the relative position of the parties is such as prima facie to raise /the presumption of fraud/, the transaction cannot stand unless the person claiming the benefit of it is able to repel the presumption by contrary evidence, proving it to have been in point of fact fair, just, and reasonable.[2]

His Lordship continued:

> This principle of relief is not limited to transactions with expectants. 'It has been extended to all cases in which the parties to a contract have not met upon equal terms'"[3]

Unlike lunacy or mental incompetency which is generally a continual state,[4] even an alcoholic has moments of sobriety. It

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1 Ibid., 405 per Fullagar J. See also M'Diarmid v. M'Diarmid (1828) 3 Bli.N.S. 374.

2 Earl of Aylesford v. Morris (1873) L.R. 8 Ch.App. 484, 491 cited in Blomley v. Ryan (1956) 99 C.L.R. 362, 386.

3 Blomley v. Ryan (1956) 99 C.L.R. 362, 386 per McTiernan J. citing from White and Tudor's Equity Cases 7th ed. (1897) vol. 1, p.313.

4 See, however, Selby v. Jackson (1844) 6 Beav. 192 where the court refused to set aside two deeds despite the fact that they were executed by the plaintiff while he was in a lunatic asylum. It was, however, proved that he understood the nature and effect of the documents and that they were perfectly fair.

is consequently not always possible to trace a contract to an actual state of intoxication. In Dunnage v. White[1] where an heir who had habits of intoxication, surrendered an unimpeachable title when sober, the court made no attempt to connect the general incapacitating habits of the heir with the execution of the deed, but maintained that

> /S/uch habits, though not constituting an absolute incapacity, lay a ground for strict examination, whether the instrument contains in itself evidence that advantage was taken.[2]

Sir Thomas Plumer M.R. held that although there was no undue influence, the fact that the heir was ignorant of his rights, dissolute and illiterate and that there was a great inequivalence in the values exchanged[3] sufficiently showed that the heir was imposed upon and that therefore the transaction could not stand.

3. Illness and other bodily disabilities

The considerations which lead to the setting aside of unfair bargains entered into by parties who suffer from a weakening of the bodily faculties are similar to those which operate in respect of the classes of mental weakness and intoxication.

The courts do not look favourably upon transactions concluded by people on their deathbed. In Willan v. Willan[4] an agreement,

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1 (1818) 1 Swan 137.

2 Ibid., 150.

3 See also M'Diarmid v. M'Diarmid (1828) 3 Bli. N.S. 374; Dunnage v. White (1818) 1 Swan 137.

4 (1814) 2 Dow 274.

unfair with regard to both the consideration and the provisions in respect of renewal, was set aside, having been obtained from a person who was on his deathbed and "in such a state of bodily and mental imbecility as rendered him incapable of transacting business which required deliberation and reflection."[1] Lord Redesdale asked

> whether, even if there had been no evidence of imbecility, such an agreement, made under such circumstances, would not be set aside on the ground of surprise and misapprehension.[2]

And in Forshaw v. Welsby[3] the court set aside an irrevocable settlement on his family, made by a person in extremis. Sir John Romilly M.R. held that despite the fact that no undue influence or pressure was used by the relations an agreement which could function as improvidently as this one would not be allowed to stand unless the person making the settlement was able to form a "cool and uncontrolled judgment with respect to his position."[4] In most of the transactions involving gifts or settlements for which no consideration is given in return the unfairness lies in the fact that the donor or person making the settlement divests himself permanently of the whole or a large portion of his property.[5] Consequently, where the disposition contains a power of revocation, that will generally be sufficient to negative the charge that the dispositor has been unfairly taken

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1 Ibid., from headnote.

2 Ibid.

3 (1860) 30 Beav. 243.

4 Ibid., 252

5 See, for example, Anderson v. Ellsworth (1861) 3 Giff. 154.

advantage of. A disposition will, however, be set aside, notwithstanding the inclusion of a revocation clause, where such power is likely to be useless, as for example, where the transaction is concluded a few hours before the death of the person making the gift or the settlement.[1]

The courts also take account of lesser physical defects such as deafness[2] and infirmity caused by old age.[3]

In Longmate v. Ledger an old man of feeble intellect sold his property at a great undervalue to one of his creditors. Sir John Stuart V.C. declared:

> By the settled doctrine of this Court, in order to have a valid contract or conveyance of property there must be a reasonable degree of equality between the contracting parties. In this case it is established by the evidence that the property was sold for a price greatly below the value. This circumstance, of itself, might not be sufficient to invalidate the transaction. But when there is the additional fact that the vendor was a man advanced in years and known to be of a weak and eccentric disposition, and at the time of the sale was without the assistance of a disinterested legal adviser, there exists on the whole case such an inequality between the contracting parties that it is to my mind impossible for the Court to recognise the claim of the Defendant to hold his property under the contract, except as a security for the payment of the monies which have actually been advanced.[4]

The old man was so peculiar, the Vice-Chancellor continued, that anyone contracting with him would have to show that he had not taken unfair advantage of his weakness and that he had been paid a fair price.[5] Mere old age is, however, not sufficient to show that a

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1 See Fane v. Duke of Devonshire (1718) 6 Bro.P.C.137.

2 Ferres v. Ferres (1708) 2 Eq. Ca.Ab.695; Torrance v. Bolton (1872) 8 L.R.Ch.App. 118.

3 Anderson v. Ellsworth (1861) 3 Giff. 154; M'Diarmid v. M'Diarmid (1828) 3 Bli.N.S. 374; Longmate v. Lodger (1860) 2 Giff. 157; Blachford v. Christian (1829) 1 Kn.73; Grealish v. Murphy [1946] I.R.35; Blomley v. Ryan (1956) 99 C.L.R.362.

4 (1860) 2 Giff. 157, 163.

5 Ibid., 164.

person is unable to protect his interests[1] and is consequently a target for imposition. Old age is, therefore, generally used as evidence of impaired bargaining power in conjunction with other examples of personal inequality such as mental impairment or intoxication. In these cases the test used to determine whether a party's bargaining power was in fact impaired by his disability was to ask whether he or she understood the nature and effect of the transaction.

In the cases concerning agreements obtained by medical doctors or dentists from ill patients in return for professional care the courts have been even more ready to grant relief. In Popham v. Brooke[2] Sir John Leach M.R. declared that even if the patient had understood the nature and effect of the transaction the court would not have countenanced an agreement where the defendant was aware that the patient would not live long and thus knew that the consideration which he would be giving in return was grossly inadequate. And in Dent v. Bennett, Lord Cottenham L.C. said:

> ... when I find an agreement, so extravagant in its provisions, secretly obtained by a medical attendant from his patient, of a very advanced age, and carefully concealed from his professional advisers and all other persons, and have it proved that the habits, views, and intentions of the testator were wholly inconsistent with those provisions, I cannot but come to the conclusion that the medical attendant did obtain it by some dominion exercised over his patient. How it was effected, whether by direct fraud, or by what other means, the Defendant has, by the secrecy of the transaction, prevented my having any direct testimony. By that he cannot profit.[3]

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1 Lewis v. Pead (1789) 1 Ves. 19.

2 (1828) 5 Russ. 8.

3 (1839) 4 My. & Cr. 269, 277. See also Allen v. Davies (1850) 4 De G. & S. 133.

These cases will now probably fall within the category where undue influence is presumed from the relationship of the parties.

Similar considerations apply where the defendant, aware that the plaintiff is dying, buys a reversionary interest from him for an amount which, because of the fact that the plaintiff is dying and that he is not, as he himself believes, a good life, is grossly below the true value in the circumstances.[1]

(iiib) Impaired bargaining power caused by inferior social status or position of one party

Courts have also given relief where unfair advantage had been taken of a bargaining weakness which resulted from a person's status, material circumstances or lack of education. More specifically, it has been recognised that a disparity in bargaining strength might be caused by poverty, illiteracy or a general lack of education and that the young, sailors and generally the underprivileged, should be given judicial protection.

It may seem curious today to regard being a sailor as a mark of bargaining weakness. Yet, in the eighteenth and early nineteenth centuries courts frequently adopted a paternalistic attitude towards sailors. In How v. Weldon and Edwards,[2] Sir Thomas Clarke M.R. maintained that sailors should be regarded in the same light as heirs because they are "a race of men, loose and unthinking, who will almost for nothing part with what they have acquired."[3] And

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1 Davies v. Cooper (1840) 5 My. & Cr. 270.

2 (1754) 2 Ves. 516.

3 Ibid., 518. Also Baldwin & Alder v. Rochford (1748) 1 Wils. K.B. 229; Taylour v. Rochfort (1751) 2 Ves. 281.

in Stilwell v. Wilkens[1] a purchase at great undervalue was set aside because it was "procured from a person who could not possibly judge for himself; the young man was a common sailor, lately come ashore, and much pressed for money."[2]

Although a sailor was regarded as per se at a disadvantage vis-à-vis his counterparty that fact was not in itself a sufficient ground for relief. In Griffith v. Spratley[3] a "sailor in distressed circumstances and oppressed by his creditors"[4] sold his interest in an estate to a "broker living on the estate, and understanding the value of it."[5] Yet Eyre L.C.B. refused relief because the undervalue complained of was so small that it was impossible "to infer an undue advantage (which implies intention) taken of the necessities of a man, such as to authorize the Court to relieve on the ground of fraud and imposition."[6]

The cases in which sailors as a group were given special protection were few and they generally also provide evidence that the sailor was financially distressed or that he entered into the contract under economic necessity, so that the cases could equally have proceeded on these grounds. Although the policy of singling out sailors as particularly worthy of protection soon disappeared,

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1 (1821) Jac. 280.

2 Ibid., 282.

3 (1787) 1 Cox C.C. 383.

4 Ibid., 388.

5 Ibid.

6 Ibid., 390

the cases were important in that they indicated the willingness of the courts to extend their protection not only to individuals, but to a whole class of people, if they thought that they were by nature unable to take care of their interests or that they were liable to be imposed upon.

Similar protection was given to the young. In Nevill v. Snelling[1] a young man began borrowing money at an exorbitant rate of interest from a moneylender when he was still a minor. The transactions continued after he had reached majority. The plaintiff was not an expectant heir of the type which fell within the scope of the previously examined branch of fraud, but had general expectations from a wealthy father. Nevertheless, Denman J., in setting aside the transactions except insofar as they should stand as security for the sums actually advanced plus 5 per cent interest, stated that there was little difference in principle between the transactions in that case and the catching bargains with heirs from which equity habitually relieved. His Lordship admitted that it did not follow

> ... because the transactions may have been most usurious, that they ought to be set aside, or that the Defendant ought to be deprived of the bargain into which he may have led a foolish and improvident young man, provided it really was a bargain understood by both parties, and entered into under such circumstances as to shew mere folly and extravagance on the one side, and mere usury on the other.[2]

But relief could be given

> upon the general principles of Equity, which lay it down that unfair and unconscionable dealings with a person whose position renders him too weak to resist rapacity, and avarice, and unfair dealing ... ought to be repressed.[3]

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1 (1880) 15 Ch.D. 679.

2 Ibid., 701.

3 Ibid., 705.

However, the majority of cases in this category has been concerned with weakness arising from such factors as poverty and humbleness of position[1], illiteracy or general lack of education[2]. The relevance to modern law of some of these factors has recently been examined in two cases, Creswell v. Potter[3] and Backhouse v. Backhouse.[4] In Creswell v. Potter, a wife who was in the process of getting a divorce executed a deed of release and conveyed, at a considerable undervalue, her interest in premises of which she and her husband were joint tenants, to her husband. The wife subsequently brought an action, claiming that the release should be set aside. Megarry J., in granting the wife's request, accepted as a correct exposition of the law,[5] Kay J.'s statement in Fry v. Lane that

> /T/he circumstances of poverty and ignorance of the vendor, and absence of independent advice, throw upon the purchaser, when the transaction is impeached, the onus of proving, in Lord Selborne's words, that the purchase was 'fair, just, and reasonable'.[6]

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1 See, for example, Clarkson v. Hanway (1723) 2 P.Wms. 203; Proof v. Hines (1735) Cas. Temp. Talb. 111; Taylour v. Rochfort (1751) 2 Ves. 281; Evans v. Llewellin (1787) 1 Cox C.C.333; Griffith v. Spratley (1787) 1 Cox 383; Baker v. Monk (1864) 4 De G.F. & J.401; Cockell v. Taylor (1852) 15 Beav. 103; Clark v. Malpas (1862) 4 De G.F. & J. 401; Prees v. Coke (1871) 6 L.R.Ch.App. 645; Fry v. Lane (1888) 40 Ch.D.312.

2 See, for example, Proof v. Hines (1735) Cas.Temp. Talb.111; Garvey v. McMinn (1846) 9 Ir.Eq. 526; Clark v. Malpas (1862) 4 De. G.F. & J. 401.

3 /1978/ 1 W.L.R. 255.

4 /1978/ 1 W.L.R. 243.

5 /1978/ 1 W.L.R. 255, 257.

6 (1888) 40 Ch.D. 312, 322. The statement by Lord Selborne L.C. was made in Earl of Aylesford v. Morris (1873) 8 Ch.App. 484, 491.

As social conditions today were different from those prevailing when Fry v. Lane was decided Megarry J. suggested that "member of the lower income group"[1] now be substituted for "poor" and "less highly educated"[2] take the place of "ignorant". However, these were not the only circumstances which would invoke the aid of equity: "circumstances of oppression or abuse of confidence"[3] might also be sufficient.

Megarry J. furthermore accepted that the wife, who was a Post Office telephonist, with slender means and little savings, fell within the category of the less highly educated. And although he did not doubt her skill as a telephonist, he thought that in the context of property transactions generally, and the execution of conveyancing documents in particular, she could properly be described as "ignorant".[4] It is therefore clear that it is not necessary to prove an all-pervading ignorance - it is merely required that the plaintiff be inexperienced in the context of the particular transaction.

In Backhouse v. Backhouse[5] the court had to deal with a similar problem and although the issue was eventually decided on other grounds, Balcombe J. accepted the principles set out in Creswell v. Potter. In addition, his Lordship stated that emotional strain might also be considered as a mark of inequality.[6]

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1 /1978/ 1 W.L.R. 255, 257.
2 Ibid.
3 Ibid.
4 Ibid., 258.
5 /1978/ 1 W.L.R. 243.
6 Ibid., 251.

Why do the poor, the humble and other similarly disadvantaged parties merit protection? Initially it was said that the courts intervened because such people were less able to protect themselves against oppression or imposition.[1] In the second half of the nineteenth century the focus of the courts was transferred from the specific weakness of the party to the unequal positions of the contracting parties or to the disparity in bargaining strength between them.[2] In substance there was no difference between the earlier and the later approaches, except that the latter indicated a wider perspective on the part of the courts. Central to both was the notion that where there existed between the parties a great disparity in the respective levels of knowledge, judgment, experience and general commercial sophistication, the party in the inferior position was, in the view of the courts, more liable to be taken advantage of. Such parties were regarded as at a disadvantage vis-à-vis more affluent and commercially experienced parties with regard to both understanding the nature and effect of the trasaction and the negotiation of the terms.

It is clear that in this area, just as in the category dealing with a party's bodily and mental weakness, a lack of understanding or ignorance of the issues involved and the inequality between the parties were closely interrelated and were jointly caused by the plaintiff's general station in life. The plaintiff's lack of understanding or ignorance usually took the form of an ignorance

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1 Proof v. Hines (1735) Cas.Temp.Talb. 111; Evans v. Llewellin (1787) 1 Cox, C.C.333.

2 Baker v. Monk (1864) 4 De G.J. & S.388; Howley v. Cook (1873) I.R.8 Eq. 570; Fry v. Lane (1888) 40 Ch.D.312; Slater v. Nolan (1876) I.R.11 Eq.367; Earl of Aylesford v. Morris (1873) L.R.8 Ch.App.484; Nevill v. Snelling (1880) 15 Ch.D.679; O'Rorke v. Bolingbroke (1877) 2 App.Cas.814.

about his existing rights or about the effect of the transaction which he concluded.[1] The central question was thus the extent to which a plaintiff so afflicted would be allowed to rely on his ignorance in an action for relief from an unfair contract.

The case of Evans v. Llewellin[2] illustrates the length to which the courts have been prepared to go in protecting the humble and underprivileged who act in ignorance and inexperience from unfair bargains. Plaintiff, a person "in mean circumstances", received two hundred guineas for the sale of his property of which the actual value was £1,700. The defendant informed the plaintiff of this fact and asked him to take some time considering the deal and discuss it with friends. He refused and insisted on executing it immediately. Sir Lloyd Kenyon M.R., in relieving plaintiff from the agreement, laid great stress upon the fact that he was poor and unaware of his rights and said that

> the party was taken by surprise; he had not sufficient time to act with caution; and therefore though there was no actual fraud, it is something like fraud, for an undue advantage was taken of his situation. The cases ... all proceed on the same general principle, and establish this, that if a party is in a situation, in which he is not a free agent, and is not equal to protecting himself, this Court will protect him.[3]

It has to be remembered, however, that the mere fact that a party did not understand a transaction did not necessarily lead to relief being given by the courts. There are many cases where a person,

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1 Hobert v. Hobert (1683) 2 Ch.Ca. 159; Preston v. Wasey (1697) Pr. Ch. 76; Taylour v. Rochfort (1751) 2 Ves. 281; Strachan v. Brander (1759) 1 Ed. 303; Evans v. Llewellin (1787) 1 Cox C.C.333; Sturge v. Sturge (1849) 12 Beav. 229; Summers v. Griffiths (1866) 35 Beav. 27; Fry v. Lane (1888) 40 Ch.D. 312; Howley v. Cook (1873) I.R.8 Eq. 570.

2 (1787) 1 Cox C.C. 333.

3 Ibid., 340.

while not suffering from a bargaining handicap which places him at a disadvantage vis-à-vis his counterparty, is induced into a contract which he does not understand. Unless the courts regarded his insufficiency of understanding as in itself a mark of inequality between the parties, the problem was dealt with under the principles of mistake and not equitable fraud.

(iiic) Impaired bargaining power resulting from economic necessity and distress

There have also been cases which support the view that where a necessitous or financially distressed party concluded a contract and such necessity was exploited so that the counterparty gained an unfair advantage, the courts would intervene to set aside the contract. Chancery courts often referred to contracts of this nature as "oppressive" bargains.[1]

In Pickett v. Loggon,[2] Lord Chancellor Eldon was not prepared to state affirmatively whether a contract by which a "valuable property had been acquired" for a sum that was

> very inadequate, ... would have been reached by the doctrine of this Court; protecting, upon public principles, persons in distress; who, ... acting under the influence of that distress, though with knowledge of the circumstances, are to have the same protection, as if they were entirely ignorant: being compelled by hard necessity.[3]

Lord Eldon's approach was over-cautious. Necessity and economic distress had by that time long been recognised as evidence of

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1 See, for example, Lawley v. Hooper (1745) 3 Atk. 278, 279.

2 (1807) 14 Ves. 215.

3 Ibid., 240.

inequality between the parties, and as early as 1745 Lord Hardwicke had declared that "wherever /the Chancery courts/ have found the least tincture of fraud in any of these oppressive bargains, relief hath always been given."[1]

The nineteenth century provided many cases where a party's necessity or distress was a factor which induced the courts to relieve from an unfair contract. In Wood v. Abrey[2] two reversioners had sold an estate worth £1,600 for £400. Sir John Leach V.C., after stating that inadequacy of price was not in itself a sufficient basis for relief, said:

> But a Court of Equity will inquire whether the parties really did meet on equal terms; and if it be found that the vendor was in distressed circumstances, and that advantage was taken of that distress, it will avoid the contract.[3]

The grounds upon which the courts proceed was clearly stated in the important case of Barret v. Hartley.[4] The plaintiff had filed a bill to set aside a memorandum stipulating for a large sum to be paid to the defendant as a bonus for acting as trustee and for advancing certain monies to the plaintiff and his father. The plaintiff averred that the bonus was not owed and that the memorandum was only agreed to because of their financial distress. Sir John Stuart V.C., in setting aside the memorandum, held:

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1 Lawley v. Hooper (1745) 3 Atk.278, 279. See also Maskeen v. Cole (1733) 2 Madd. 42ln. where the court asserted that had the very necessitous plaintiff not subsequently confirmed the contract, relief would have been given; Stanhope v. Cope (1741) 2 Atk. 231.

2 (1818) 3 Madd. 417.

3 Ibid., 423.

4 (1866) L.R.2 Eq. 789.

> In order to render a contract, or an agreement of any kind, binding, there must be the assent of both parties to the agreement under such circumstances as to shew that there was no pressure - no influence existing of a kind to make the assent an imperfect assent, or an assent which, under other circumstances, would have been refused. If the assent to the agreement is not an assent given under such circumstances as that both parties are on an equal footing, and the agreement one perfectly free from any influence or pressure, in the eye of this Court, it is not an assent sufficient to constitute an agreement.[1]

The Vice-Chancellor added that although the usury laws had been repealed that only meant that the courts would now employ the established principles of equity to prevent the exaction of any advantage from a man under grievous necessity and want of money.[2]

The necessity or distress complained of has generally been of a financial nature. This explains the fact that so many of the relevant cases involved moneylending transactions, clothed as contracts of sale,[3] or other transfers in return for cash.[4] It was not necessary to show that the plaintiff was generally poor, although that would, of course, often have been the case.

In the previous category financial need and poverty were indicative of the fact that a party was likely to be commercially unsophisticated and thus often less able to understand the transaction

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1 Ibid., 794-795.

2 Ibid., 795. See also Ford v. Olden (1867) L.R.3. Eq. 461; Butler v. Miller (1867) I.R. 1 Eq. 195.

3 See, for example, Pickett v. Loggon (1807) 14 Ves. 215; Butler v. Miller (1867) I.R. 1 Eq. 195; Lawley v. Hooper (1745) 3 Atk. 278; Wood v. Abrey (1818) 3 Madd. 417.

4 See, for example, Maskeen v. Cole (1733) 2 Madd. 42ln; Stanhope v. Cope (1741) 2 Atk. 231; Ramsbottom v. Parker (1821) 6 Madd. 5.

or to protect himself in the bargaining process. Here financial necessity or distress was regarded as evidence that a party was compelled to enter into a contract even if he realized that the terms were harsh or oppressive. Some commentators have construed the fact that an unfair advantage has been taken of a person in dire financial need as an example of economic duress, the duress consisting in the defendant's refusal to contract on fair terms.[1] Such a formulation involves a considerable obfuscation of the actual processes of the court. The courts have given relief in these cases not because of economic duress exerted by the defendant, but because the plaintiff's financial need compelled him to enter into the unfair agreement. Although the dividing line between the two interpretations of equity's jurisdiction is thin, it is suggested that a formulation in terms of equitable fraud gives a more accurate reflection of the considerations of which the courts took account and should thus be accepted at the expense of a formulation in terms of economic duress.

Although "necessity" occurred mostly in economic form that was not the only type of necessity or distress of which the courts took note. A party's geographical position, for example the fact that he concluded the contract while he was in prison, has also been recognised as a factor which showed up the inequality between the parties.[2] A person might also, in addition to his financial need,

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1 See, for example, J. Dalzell, Duress by Economic Pressure II (1942) 20 N.C.L. Rev. 341, 356-361.

2 Lawley v. Hooper (1745) 3 Atk. 278; Barnard v. Flint (1796) 3 Anst. 734n.

suffer from one of the bargaining handicaps already examined. Such a fact would, of course,have rendered judicial protection even more imperative.

The courts have never made a serious attempt to define the economic need or distress which was required for judicial intervention and in most of the cases they have regarded their task as complete once they had stated that a plaintiff was "necessitous" or "distressed". Nevertheless, it does not seem as if it was necessary to prove that unless the plaintiff concluded the contract he would have faced economic ruin - a temporary shortage of cash with which to pay pressing creditors often appeared to constitute sufficient "necessity". The transactions were frequently attempts to capitalise assets in order to pay gaming creditors.[1]

"Necessity" could also be found where the purpose for which money was needed was regarded as proper by the courts. In Cockell v. Taylor,[2] a man who needed money for the purpose of prosecuting a claim in a fund borrowed £1,000 from a solicitor. One of the terms of the transaction was that he should buy a plot from the latter for £6,000 - this sum turned out to be ten times more than the value of the land. In order to complete the deal the borrower mortgaged his claim in the fund for £6,000. Sir John Romilly M.R. declared that the inadequacy of the consideration coupled with the circumstances that this was the only way in which the necessary money could be

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1 Stanhope v. Cope (1741) 2 Atk. 231.

2 (1852) 15 Beav. 103.

raised and that the borrower was almost illiterate, were sufficient reasons to set aside the transaction - "I am of opinion that this was a transaction in which advantage was taken of the necessities of the plaintiff."[1]

It was not necessary to show that the pressure to enter into the particular contract originated from the defendant. The mere fact that he exploited an already existing urgent need was sufficient reason to set the agreement aside.

In this jurisdiction, unlike the cases involving economic duress, there has been no attempt to determine whether the necessitous party had an alternative means of alleviating his need. Indeed, in Gwynne v. Heaton,[2] where a young married man who needed money urgently, entered into a disadvantageous bargain, the fact that he had hawked around his reversionary interest was regarded as relevant only in showing that he was in extreme necessity, and in Earl of Aylesford v. Morris,[3] relief was given notwithstanding the fact that it was the plaintiff who had made the offer.

Standard of Substantive Fairness

The question when a contract would be so unfair that a party would be relieved from it depended upon the type of contract involved. A distinction has to be drawn between those that involved

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1 Ibid., 116.

2 (1778) 1 Bro. C.C.1.

3 (1873) L.R.8 Ch.App. 484.

an exchange of values between the parties and voluntary dispositions or settlements. In both cases, however, the contract had to be unfair at its conclusion. It would have been of no avail to a party if a perfectly fair transaction later became unfair.[1]

Where the transaction involved an exchange, such as a purchase and sale, moneylending, or a lease, the fairness was generally tested by comparing the value of the respective performances.[2]

In evaluating the object of a sale the courts generally accepted the market value - where that was available - as the proper yardstick.[3] They, quite realistically, were not prepared to place a value upon the subject-matter which was unattainable. Nevertheless, the measurement of the value was objective. The courts took into account neither sentimental value nor facts such as that a party had been unsuccessfully hawking around his interests at a certain price.[4] The process was, on the whole, unsophisticated - although professional evaluators might have differed about the market value of a particular interest or property the courts accepted that there was a market value and not different ones depending upon the characteristics of the seller or purchaser or the circumstances surrounding the transaction.[5] At the same time it must be recognised that the courts, by basing their evaluation on the market price, took some account of commercial reality.

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1 Mortimer v. Capper (1782) 1 Bro. C.C.156; Ramsbottom v. Parker (1821) 6 Madd. 5.

2 See, for example, Creswell v. Potter [1978] 1 W.L.R.255; M'Diarmid v. M'Diarmid (1828)3 Bli.N.S. 374.

3 See, for example, Garvey v. McMinn (1846) Ir. Eq. 526; Slator v. Nolan (1876) I.R.367; Cockell v. Taylor (1852)15 Beav. 103.

4 Earl of Aylesford v. Morris (1873) L.R. 8 Ch. App. 484.

5 Cf. the statement by the Lord Keeper in Batty v. Lloyd (1682) 1 Vern. 141 that necessitous people must necessarily sell cheaper than others.

The question when the disparity between the value of the respective performances was so great as to justify relief was wholly in the discretion of the courts and it was therefore impossible to lay down any clear guidelines. It was obviously not necessary that the disparity be so great as "to shock the conscience" as that would in itself have led to an inference of fraud.[1]

The risk incurred by the benefiting party was of course a factor that could influence the decision as to whether a disparity in exchange was justified or not. As was the case under catching bargains with expectant heirs, the courts here took little account of risk.[2] That could partly be due to the fact that as the contracts involved were generally not "futures" agreements there was little risk to be run. Risk was a greater factor in moneylending and mortgage transactions, but even there it played a very minor role although the courts were not unmindful of it.[3] However, when it was taken into account it was generally done negatively - to show that because a claim was well secured there was no risk.[4]

Risk was, however, a factor which could not be monetized easily and to determine the importance of risk in the exchange it was necessary to look at the transaction as a whole. There are some indications that where the disparity in bargaining strength between the parties was great a small disparity in values exchanged would be sufficient for relief, and vice versa. On the whole, however, the contracts re-

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1 Gibson v. Jeyes (1801) 6 Ves. 266, 273.

2 See, however, Gibson v. Jeyes, supra.

3 See Cockell v. Taylor (1852) 15 Beav. 103; Nevill v. Snelling (1880) 15 Ch.D. 679.

4 Baldwin and Alder v. Rochford (1748) 1 Wils. K.B. 229.

lieved from exhibited gross disparity, often to the rate of 2 to 1, or more.[1]

Although most of the cases during this era were concerned with the level of exchange, that was not the only area in which unfairness could lie. A later case which concerned moneylending, Howley v. Cook,[2] also placed great emphasis on other terms which were "unprecedented" and oppressive to the borrower.

In transactions which did not involve an exchange of values such as voluntary dispositions the standard of fairness was, of course, different. In Phillips v. Mullings,[3] Lord Hatherley L.C. expressed the opinion that the validity of those agreements depended upon the facts peculiar to each of them. Nevertheless, it was clear from the caselaw that the courts regarded any unusual or abnormal terms with grave suspicion and would set aside any contract containing them unless they were convinced that the person making the donation was aware of the terms and understood them when he executed the transaction.[4] What was "unusual" or "abnormal" depended on the mores of the community at the time. A deed which divested the donor of all his property leaving himself and his dependants destitute or which, without apparent reason, settled all his property on people other than the natural objects of his bounty, was not easily countenanced.[5]

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1 Wood v. Abrey (1818) 3 Madd. 417 - buyer paid only a quarter of the value; Cockell v. Taylor (1852) 15 Beav. 103 - buyer paid ten times more than the value. In Butler v. Miller (1867) I.R. 1 Eq. 195 Lord Walsh M.R. said that in most cases a sale at half-price would usually be regarded as unfair in the sense here meant.

2 (1873) I.R. 8 Eq. 570. One of the terms of which the court disapproved stipulated that the moneylender could sell certain property which served as security for the loan without notifying the borrower.

3 (1871) 7 L.R. Ch.App. 244.

4 Ibid.; Coutts v. Acworth (1869) 8 L.R. Eq. 558; Phillipson v. Kerry (1863) 32 Beav. 628; Anderson v. Ellsworth (1861) 3 Giff.154.

5 Ibid.

Remedies

When it was found that a weak and necessitous party had been taken advantage of the court set aside the contract. Where the transaction in question was a financing or moneylending agreement it was usually only set aside upon payment of the actual sum advanced, plus interest generally at 5 per cent, and if it was a sale of property which had already been transferred it was returned to the plaintiff who had to reimburse the defendant for any money spent on the property. Where there was any misconduct or unfair dealing on the part of the defendant he had to pay the costs of the action, otherwise this was usually borne by the plaintiff. The courts were, on the whole, disinclined to reform contracts which they found to be unfair because, as Lord Eldon correctly observed in Pickett v. Loggon,[1] the parties would probably never have concluded the agreement had the terms been different.

(iv) Undue Influence

The power of the courts to set aside a transaction on the ground of undue influence constitutes one of the most important exceptions to the principle of freedom of contract. Undue influence was firmly established as an independent ground for striking down a contract in Huguenin v. Baseley[2], but the principles on which it was based were recognised as early as the beginning of the eighteenth century.[3] In

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1 (1807) 14 Ves. 215, 242.

2 (1807) 14 Ves. 273.

3 Kingsland v. Barnewell (1706) 4 Bro. P.C. 154; Osmond v. Fitzroy (1731) 3 P.Wms. 129; Bennet v. Vade (1742) 9 Mod. 312; Morris v. Burroughs (1737) 1 Atk. 398.

the earlier cases it was apparently regarded as a species of the previously discussed branch of equitable fraud.

There is, in fact, a close relationship between fraud which is inferred from the fact that advantage has been taken of a party's weakness and undue influence, especially if in the latter case the disadvantaged party also suffered from a bargaining handicap which would have led to inequality between the contractual parties.[1] The distinction between the two lies in the fact that undue influence can only be found where one party occupies a position of confidence or influence vis-à-vis the other.[2] The essence of both remedies lies in the fact that relief will only be granted where an unfair advantage was taken of the situation - in the one case, of the inequality between the parties and in the other, of the relation of influence which existed between them. As in the case of fraud between unequal parties, undue influence can be found irrespective of whether the contract involved was "a gift, a purchase at an undervalue, and a sale at an excessive price."[3]

Undue influence has never been clearly defined.[4] The result is that the term has been used in different senses, to include not only

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1 See generally, M.D. Green, Fraud, Undue Influence and Mental Incompetency (1943) 43 Col. L. Rev. 176.

2 Ibid., 180. See also W.H.D. Winder, Undue Influence and Coercion (1939) 3 Mod. L. Rev. 97, 98.

3 Tufton v. Sperni (1952) T.L.R. 516, 526 per Jenkins L.J.

4 Re Brocklehurst [1978] 1 All E.R. 767, 783 per Bridge L.J.

the exercise of influence but also compulsion. However, Winder[1] has convincingly argued that the term undue influence implies affection and attachment and not coercion. A person acting under undue influence assents to a contract because he wishes to gratify the desires of another,[2] not because he is coerced into giving his assent.

The courts distinguish between two classes of influence:

(a) If, at the time of, or shortly before, the conclusion of the contract there existed between the parties a special confidential relationship by reason of which the one party necessarily had influence over the other, a presumption is raised that the gift or contractual advantage was induced by the exercise of undue influence and the court will set aside the contract unless it is proved that it was "the spontaneous act of the donor acting under circumstances which enabled him to exercise an independent will and which justifies the Court in holding that the gift was the result of a free exercise of the donor's will."[3] A court may thus set aside a contract even though there is no proof of actual undue influence. The court interposes not on the ground of any wrongful act by the defendant but because of public policy.[4] A presumption of undue influence is raised because the one party is by reason of the general confidence which is reposed in him by the other, in a position to take an unfair advantage of that other[5] and because

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1 Winder, op. cit. There is, furthermore, a difference in the meanings given to undue influence in probate and equity. In the former the influence must "amount to force and coercion destroying free agency - it must not be the influence of affection and attachment": Williams v. Goude (1828) 1 Hag. Ecc. 577,581 per Sir John Nicoll.

2 Williams v. Goude (1828) 1 Hag. Ecc. 577, 581.

3 Allcard v. Skinner (1887) 36 Ch.D. 145, 171 per Cotton L.J.

4 Ibid.

5 Treitel, Law of Contract, 309.

proof of undue influence in respect of the contract in question may be difficult where influence necessarily exists.[1] Where the relationship between the parties is such that undue influence is presumed the contract will only be allowed to stand if there is proof of the removal of that influence.[2]

The presumption can be rebutted by showing that the plaintiff was assisted in the transaction by an independent and competent adviser[3] although that is by no means the only way.[4] In some cases the standard which this advice must attain has been set very high. In Bullock v. Lloyds Bank Ltd.,[5] for example, Vaisey J. said that a settlement of certain property on trustees by a father on behalf of his daughter would be upheld

> if executed under the advice of a competent adviser capable of surveying the whole field with an absolutely independent outlook, and who explains to the intending settlor, first, that she could do exactly as she pleased, and, secondly, that the scheme put before her was not one to be accepted or rejected out of hand but to be discussed, point by point, with a full understanding of the various alternative possibilities.[6]

The courts seem to be particularly strict where donations are concerned and they require very clear evidence that the donor formed his intention freely and not under the influence of the donee.[7] Where

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1 Re Craig [1971] Ch. 95, 104.

2 Ibid., 105.

3 Allcard v. Skinner (1887) 36 Ch.D. 145, 190.

4 Inche Noriah v. Shaik Allie Bin Omar [1929] A.C. 127, 135.

5 [1955] Ch. 317.

6 Ibid., 326.

7 Wright v. Carter [1903] 1 Ch. 27, 50.

a donor had no independent advice, but the amount of the gift was small, the transaction will not necessarily be set aside.[1] "But if the gift is so large as not to be reasonably accounted for on the ground of friendship, relationship, charity, or other ordinary motives on which ordinary men act, the burden is upon the donee to support the gift."[2] This does not, however, mean that the character and attitudes of the donor can be ignored.[3]

The presumption can also be rebutted by showing that in a transaction for consideration the bargain was a fair one.[4] Indeed, where a solicitor contracts with a client the bargain will be set aside on the ground merely of undervalue.[5]

Transactions between the following people have been adjudged to give rise to a presumption of undue influence: parent and child,[6] solicitor and client,[7] doctor and patient,[8] spiritual adviser and follower,[9] trustee and beneficiary.[10] However, no limitation has been placed on the types of relations which might fall within this category - in fact the courts have been "careful not to fetter this useful jurisdiction by defining the exact limits of its exercise."[11]

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1 Allcard v. Skinner (1887) 36 Ch.D. 145, 185.

2 Ibid., per Lindley L.J.

3 Re Brocklehurst [1978] 1 All E.R. 767, 783.

4 Wright v. Carter [1903] 1 Ch. 27, 54-55; Kingsland v. Barnewell (1706) 4 Bro. P.C. 154.

5 Edwards v. Meyrick (1842) 2 Hare 60, 70; Wright v. Carter [1903] 1 Ch. 27.

6 Bullock v. Lloyds Bank Ltd. [1955] Ch. 317.

7 Edwards v. Meyrick (1842) 2 Hare 60.

8 Re Craig [1971] Ch. 95.

9 Allcard v. Skinner (1887) 36 Ch.D. 145.

10 Plowright v. Lambert (1885) 52 L.T. 646.

11 Tate v. Williamson (1866) 2 Ch.App.55,61 per Lord Chelmsford L.C.

The evidentiary advantage of bringing one's case within this class of relationship is clear and any plaintiff is free to attempt to bring his case within its ambit. A relation of that class will be found "/w/herever two persons stand in such a relation that, while it continues, confidence is necessarily reposed by one, and the influence which naturally grows out of that confidence is possessed by the other."[1] In Tufton v. Sperni,[2] Jenkins L.J. warned that one should not work backwards from the fact of an unconscionable bargain and construct a fiduciary relationship between the parties through which to set it aside, but that, it seems, is precisely what has happened in some cases where the relationship between the parties was not one of those from which the presumption would ordinarily have arisen. In Re Craig, Ungoed-Thomas J. said:

> what has to be proved to raise the presumption of undue influence is first a gift so substantial (or doubtless otherwise of such a nature) that it cannot prima facie be reasonably accounted for on the ground of the ordinary motives on which ordinary men act.[3]

The fact that the fairness of a contract plays a major role in determining whether a relation is of a type that gives rise to a presumption of undue influence may also be a reason why the courts have found it so difficult and been so unwilling to lay down clear guidelines as to which relationships fall in the one, and which in the other category.

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1 Ibid.

2 (1952) T.L.R. 516, 530.

3 /1971/ Ch. 95, 104.

(b) Where there is no special confidential relationship between the parties the plaintiff may yet bring evidence to show that the defendant was in a position of influence over him, which he used unduly to induce the plaintiff to enter into a contract which he would not otherwise have concluded. Policy does not dictate that one party should have no influence over the other, only that such influence should not be abused. There are no hard and fast rules as to the way in which undue influence may be proven. One commentator has concluded that undue influence is generally inferred from a combination of some of the following factors:[1]

(i) The plaintiff was particularly susceptible to undue influence, for example, where he was young,[2] old,[3] physically or mentally weak,[4] drunk and in need of money,[5] credulous and unbusinesslike.[6]

(ii) The opportunity to exercise undue influence existed, for example, where the facts indicate that the plaintiff was dependent upon the defendant.[7]

(iii) Factors which indicate a disposition towards exercising undue influence such as that the defendant initiated the contract.

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1 Note, (1941) 41 Col.L.Rev. 707, 717-721.

2 Osmond v. Fitzroy (1731) 3 P.Wms. 129 - plaintiff just come of age.

3 Griffiths v. Robins (1818) 3 Madd. 191 - plaintiff eighty four and almost blind.

4 Ibid.; Bennet v. Vade (1742) 9 Mod. 312.

5 Wright v. Long (1898) 14 T.L.R. 516.

6 Tufton v. Sperni (1952) T.L.R. 516.

7 Osmond v. Fitzroy (1731) 3 P.Wms. - plaintiff entrusted to defendant's care; Kingsland v. Barnewell (1706) 4 Bro. P.C. 154 - defendant the manager and standing counsel of plaintiff; Taylor v. Obee (1816) 3 Pr. 83 - defendant was friend of plaintiff's late husband.

(iv) Factors showing that the contract was in fact the result of undue influence. Here the fairness or normality of the contract is of great importance, but other factors such as the presence of independent advisers and the secrecy in which the transaction was shrouded are taken into consideration.

The dividing line between this class of case and that where undue influence is presumed is very thin and many of the factors mentioned above may also lead to a finding that a special confidential relationship existed between the parties.

While the jurisdiction against unfair contracts concluded by unequal parties waned in the late nineteenth and twentieth centuries, undue influence secured an important position as a ground on which relief from contractual obligations could be granted. The reason for this lay in the fact that undue influence, frequently portrayed as being concerned almost exclusively with the propriety of a party's consent, was more compatible with a theory of contract which professed to be interested not in the fairness of a contract but only in the quality of a person's consent to it. In reality, of course, the picture was vastly different. The principles underlying undue influence arose during a time when the Chancery courts regarded control of the fairness of contracts as a legitimate and indeed desirable practice.

Although the doctrine of undue influence is often discussed solely in terms of whether a party exercised a free will its effect remains the enforcement of a standard of substantive fairness, if only because the question whether there has been undue influence

is frequently answered by reference to the contract itself. As early as 1807 it was recognised by Lord Eldon L.C. that the contract itself was the best evidence of whether there was undue influence or not.[1] The courts have often used the yardstick of whether an honest and fair man would have acted with his property in the manner in which the person allegedly subjected to the influence had done. A fair contract has, therefore, frequently been equated with the actions of a fair and normal person and an unfair contract as the result of undue influence.

What is regarded as a fair contract will depend, as it did under the other branches of equitable fraud, on the mores of the community. A grossly unequal bargain has always been viewed as unfair or at least abnormal. This was generally true even during the height of nineteenth century laissez-faire and has become even more so today. Where gifts are concerned it is more difficult to lay down objective standards of fairness. Although the "normality" of the transaction plays a role here as well it is probably true to say that the courts will require stronger evidence in such a case that the donor exercised a "free will" than they do in the case of a contract for consideration.

Summary: Equitable fraud

The doctrine which in the eighteenth century became known as equitable fraud arose in the Chancery courts during the latter part of the seventeenth century. Although the doctrine eventually

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[1] Huguenin v. Baseley (1807) 14 Ves. 273,296.

consisted of various branches, judicial intervention was initially motivated by narrow class-based objectives: relief was given to expectant heirs who had concluded unfair bargains in anticipation of their expectancies. Soon, however, the scope of Chancery's intervention was extended to all weak and necessitous parties who had been imposed upon. Fraud was inferred from the weakness of one party coupled with the unfairness of the contract.

Equitable fraud was not greatly affected by the rise of freedom of contract, if anything it came to be applied more widely and the standard of fairness required was enforced more strictly in the nineteenth century. Rather than emphasize the specific weakness from which a party suffered, such as mental impairment or economic need, the courts began to describe as fraud all cases where a inferior bargaining position had been taken advantage of.

Early in the nineteenth century the courts held that a party who had dealt with an expectant heir and who was resisting cancellation of the agreement had to prove its fairness. This practice of transferring the burden of proof was in the late nineteenth century adopted in all cases where the parties had been bargaining from unequal positions.

Equitable fraud was not primarily concerned with whether a party had consented to a contract. Chancery's role was a regulative one. It did not interfere merely because the consideration was inadequate although where the inadequacy was gross the courts were prepared to infer fraud. Chancery intervened in order to prevent the weaker party being exploited by the stronger and relief

was given in spite of the weaker person's consent to the bargain and not because of a defective consent.

The only branch of equitable fraud which has continued to be applied widely in the twentieth century is undue influence. Although applied in a number of cases in modern times, the rest of the doctrine fell into obscurity soon after the fusion between common law and equity. In recent years it has, however, been resurrected - in a few cases in its original form, but mainly as one of the main foundations of the doctrine of inequality of bargaining power.[1] This doctrine is discussed at a later stage.

(d) Contracts concluded under pressure[2]

The case most frequently cited in this field is Williams v. Bayley.[3] Bankers, who had discovered that a son had forged his father's name as indorser on certain promissory notes, insisted on a settlement to which the father was to be a party. The latter, fearful as a result of a warning by the bankers that they had the power to have the son prosecuted for forgery, executed a mortgage on his property in favour of the bank and in return the notes were delivered up to him. Although there was never any direct threat by the bankers that they would prosecute the son, the House of Lords was, nevertheless, of the opinion that there had been an implied threat and that consequently the transaction could not stand.

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1 See Lloyds Bank Ltd. v. Bundy /1975/ 1 Q.B. 326, 336-339.

2 See generally W.H.D. Winder, Undue Influence and Coercion (1939) 3 Mod. L. Rev. 97, 110-119.

3 (1866) L.R. 1 H.L. 200.

According to Lord Westbury

> /a/ contract to give security for the debt of another ... is, above all things, a contract that should be based upon the free and voluntary agency of the individual who enters into it. But it is clear that the power of considering whether he ought to do it or not, whether it is prudent to do it or not, is altogether taken away from a father who is brought into the situation of either refusing, and leaving his son in that perilous condition, or taking on himself the amount of that civil obligation.[1]

Lord Cranworth L.C., who was also of the opinion that the contract should be set aside, referred to "this doctrine of pressure" and said:

> /I/t is not pressure in the sense in which a Court of equity sets aside transactions on account of pressure, if the pressure is merely this: 'If you do not do such or such an act I shall reserve all my legal rights, whether against yourself, or against your son.'[2]

There must be an implied threat of prosecution. In a separate concurring speech Lord Chelmsford maintained that as "the agreement /had been/ extorted from the father by undue pressure"[3] it had to be struck down. "/T/he case", his Lordship said, "comes within the principles on which a Court of equity proceeds in setting aside an agreement where there is inequality between the parties, and one of them takes unfair advantage of the situation of the other, and uses undue influence to force an agreement from him."[4]

It is clear that Lord Chelmsford did not use the term "undue influence" in its usual meaning, because he also said that

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1 Ibid., 218-219.

2 Ibid., 209.

3 Ibid., 214.

4 Ibid., 216.

"the fears of the father were stimulated and operated on to an extent to deprive him of free agency, and to extort an agreement from him for the benefit of the bankers"[1] and as Winder convincingly argued, undue influence "operates although there is true consent and even eagerness in the transaction, without anything in the nature of force."[2] Nevertheless, the tendency on the part of the courts[3] and commentators[4] to describe this equitable doctrine of pressure as a manifestation of undue influence has persisted. Salmond even called it "undue influence between strangers"[5] in a passage quoted with apparent approval by Porter J. in Mutual Finance, Ltd. v. John Wetton & Sons, Ltd.[6] His Lordship maintained that the right to avoid a contract was not limited to situations where duress was present, but depended upon "the much wider relief given on principles originally evolved in the Chancery courts under the name undue influence."[7]

However, the equitable doctrine of pressure is closer in character to common law duress than it is to undue influence, which requires the existence of a confidential relationship between the parties. And not only is the means of inducement under the "pressure doctrine" different from that which constitutes undue

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1 Ibid.

2 Op. cit., 111.

3 See, for example, Mutual Finance, Ltd. v. John Wetton & Sons Ltd. [1937] 2 K.B. 389.

4 See, for example, Treitel, Law of Contract, 271.

5 Salmond on Contracts, 259.

6 [1937] 2 K.B. 389, 394-395.

7 Ibid., 394.

influence, but as Winder indicated, the effect of the inducement on the party also differs. The nature and effect of pressure was explained by Stuart V.C. in Bayley v. Williams as follows:

> Where a power of operating on a man's fears exists, and he enters into a contract unwillingly and under the influence of that power, its existence constitutes pressure.[1]

There is thus a strong case for rejecting the terminology of Salmond and others who describe this doctrine as a form of undue influence.

The equitable doctrine enunciated in Williams v. Bailey has been applied in later cases and it is important to establish the scope of the protection which it affords. In the passage mentioned above Salmond asked:

> What forms of coercion, oppression, or compulsion amount to undue influence invalidating a contract as between strangers between whom there exists no fiduciary relation? How is the line to be now drawn between those forms of coercion or persuasion which are permissible and those which the law recognizes as unlawful and as a ground of contractual invalidity? To this question it is impossible, as the authorities at present stand, to give any definite or confident reply. In the case already cited of Kaufman v. Gerson[2] it is suggested that the line should be drawn by reference to general considerations of public policy, the question in each case being: 'Is the coercion or persuasion by which this contract was procured of such a nature that the enforcement of a contract so obtained would be contrary to public policy?' Just as a contract may be invalid because it is contrary to public policy in its substance or its purposes, so it may be invalid because it is contrary to public policy in respect of the coercive method of its procurement.[3]

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1 (1864) 4 Giff. 538, 661.

2 [1904] 1 K.B. 591.

3 Cited in [1937] 2 K.B. 389, 394-395.

And in Ellis v. Barker, Lord Romilly M.R. circumscribed the doctrine as follows:

> Coercion takes an infinite number of forms, but it may properly be thus defined: the moment that the person who influences the other does so by the threat of taking away from that other something he then possesses, or of preventing him from obtaining an advantage he would otherwise have obtained, then it becomes coercion and it ceases to be persuasion or consideration.[1]

Lord Romilly's definition of operative coercion was a wide one and encompassed pressure other than that constituted by a threat of criminal prosecution. There were, nevertheless, a few cases which might support such a view. In Ormes v. Beadel[2] a builder, urgently needing money to pay his employees who had threatened to stop work unless they were paid their wages, was forced to conclude a contract with a debtor who maintained that he would not otherwise pay his debts. Stuart V.C. set aside the agreement and said:

> Where an agreement, hard and inequitable in itself, has been exacted under circumstances of pressure on the part of the person who exacts it, this court will set it aside.[3]

Wheeler v. Sargeant[4] similarly showed that pressure, even though it was not the result of a threat of criminal prosecution might be sufficient to set aside a transaction. In that case the court allowed recovery of money paid by a beneficiary to an executor in return for a gratuitous promise. Romer J. held that although

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1 (1870) 40 L.J. Ch. 603, 607.

2 (1860) 2 Giff. 166, reversed in 2 De G.F. & J. 333, but on other grounds.

3 Ibid., 174.

4 [1893] 68 L.T. 180.

> there were no threats of any kind by the defendant, I think there was pressure in fact on his part, though not appearing in any form of words employed by him. His very position gave him the opportunity of putting pressure on the beneficiaries ... I think that this document was signed by the plaintiff partly from the fear that if he did not sign it, it would be worse for him, owing to the defendant's position.[1]

This was a very wide interpretation of equity's power of protection and corresponded more closely with the approach in those cases, discussed before, where the mere facts that the parties stood in unequal positions and the contract was unfair, were sufficient grounds for relief. Although Romer J. found that there was pressure in fact, the possibility exists that where the courts do not require evidence of any direct threat, but are prepared to infer it from the inequality of the parties' bargaining positions, the two jurisdictions may run into each other. However, unless the courts are prepared to hold, as a matter of general principle, that wherever parties who are unequal conclude an unfair contract, the weaker will be relieved from the bargain, it is better to keep the jurisdictions apart, as they cover different fact situations. The jurisdiction against equitable fraud operates where the stronger party obtains an unfair advantage by exploiting an already existing bargaining handicap of another. In the case of the doctrine of pressure, on the other hand, relief is given because one party by exerting pressure on the other caused a bargaining handicap in the latter from which he ought to be free. Nevertheless, it has to be conceded that the dividing line between the two jurisdictions is very thin.

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[1] Ibid., 183.

Despite the cases reviewed above the type of pressure which has come before the courts was most frequently caused by a threat of criminal prosecution.[1] A mere warning that criminal proceedings may be started is not enough - there must be a threat that criminal proceedings will be initiated unless the contract is concluded. In Barnes v. Richards[2], for example, a resignation and release of salary by an employee who could not explain certain errors in the accounts was not cancelled as there was no threat to prosecute him. It is not, however, always necessary that the threat of criminal prosecution should be express. Even an implied threat will suffice so long as it is clear that the contract is entered into in order to prevent prosecution. As Porter J. said in Mutual Finance Ltd. v. John Wetton & Sons Ltd.: "If the known object was to prevent the prosecution of his brother for whatever reason, that, I think, is enough."[3]

It is, furthermore, not essential for a contract to be set aside that the person against whom the threat of criminal prosecution is made should be the contractual party himself or a relative of his. The central question is whether a party entered into a contract in order to prevent the threatened prosecution and so long as that causal link exists there is no need to limit the jurisdiction of the court. As Porter J. said in the Mutual Finance case,

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1 See for example, Collins v. Hare (1828) 1 D. & Cl. 139; Seear v. Cohen (1881) 45 L.T. 589; Kaufman v. Gerson [1904] 1 K.B. 591.

2 (1902) 71 L.J.K.B. 341.

3 [1937] 2 K.B. 389, 396.

> /It is not necessary to determine the exact bounds beyond which the doctrine would not be applied, but I should myself be inclined to say that it extended to any case where the persons entering into the undertaking were in substance influenced by the desire to prevent the prosecution or possibility of prosecution of the person implicated, and were known and intended to have been so influenced.[1]

An agreement induced by threats of criminal prosecution may also be set aside on the ground that it stifles a prosecution for an offence. In that case the party seeking relief from the agreement must show not only that the conclusion of the contract prevented the criminal prosecution but that it was an implied or express term of the agreement that there should be no criminal proceedings.[2]

Unlike the common law courts which continued throughout the nineteenth century to define relievable duress in a very limited way, equity relieved from transactions even where a contract was entered into or a payment made under a threat which was not unlawful. The courts clearly felt that threats which might normally be perfectly legal could become unacceptable when used oppressively, that is when the pressure was exerted solely for the purpose of inducing a party into a contract which he was otherwise unwilling to conclude or into making a payment which was not due. Although there were a few cases involving other forms of compulsion they were comparatively isolated and the most common type of pressure which the

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1 Ibid.

2 Chitty on Contracts, section 434.

courts were called upon to deal with were threats of criminal prosecution. There can be little doubt that the courts' decision to intervene was motivated to a considerable extent by the fact that obligations had been undertaken under pressure in return for which no or only an inadequate consideration was given. To be given relief it was necessary only to establish a causal link between the pressure and the undertaking of the obligation.

5 - DURESS

Any doctrine which attempts to deal with the problem of contracts procured by pressure poses two questions: firstly, which types of pressure are improper or illegitimate, and secondly, which facts will be sufficient to establish that the pressure was a[1] reason for the party concluding the contract?

The question as to which type of pressure is improper was answered restrictively by the traditional doctrine of duress. The doctrine arose at common law as an adjunct of criminal and tort law[2] and in accordance with these origins the types of pressure which were regarded as legally relevant were limited to those which were independently wrongful, in particular actual or threatened violence against the person and unlawful imprisonment. A party who wished to avoid a contract on the ground of duress also had to show that the duress was of such intensity as to overcome a man of constant firmness. During the nineteenth century the standard of constant firmness was rejected and a new subjective test, requiring the court to establish in every case whether the pressure was such as to overcome that particular person, instituted in its place.[3] Apart from

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1 Barton v. Armstrong /1976/ A.C. 104, 119 per Lord Cross of Chelsea: "/The coerced party/ is entitled to relief even though he might well have entered into the contract if /the defendant/ had uttered no threats to induce him to do so."

2 See generally J.P. Dawson, Economic Duress - An Essay in Perspective (1947) 45 Mich. L.Rev. 253, 254-255; Goff and Jones, The Law of Restitution, 163-168.

3 Scott v. Sebright (1886) 12 P.D. 21, 24.

that relaxation the traditional doctrine of duress remained more or less unchanged for centuries. It was indeed a primitive tool giving only limited protection to a coerced party.

The position was somewhat alleviated by equity which, as we have seen, extended the ambit of relief considerably, mainly by holding that an improper use of the legal process could amount to a ground for relief.[1] After the fusion of law and equity the wider jurisdiction of the latter prevailed. In addition, the past few years have witnessed a cautious affirmation that duress in English law might include some instances of economic coercion.[2] The law

> under the influence of equity, has developed from the old common law conception of duress - threat to life and limb - and it has arrived at the modern generalisation expressed by Holmes J. - 'subjected to an improper motive for action.'[3]

The recognition that economic coercion might constitute relievable duress was the culmination of a long development which originated in the eighteenth century and earlier.

The narrow common law definition of duress belied the fact that coercion aimed at the economic interests of a party was frequently encountered in the eighteenth century. At that time, however, problems of duress arose mainly in respect of executed

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1 Duke de Cadaval v. Collins (1886) 4 Ad. & E. 858.

2 Post, 160 et seq.

3 Barton v. Armstrong [1976] A.C. 104, 121 per Lord Wilberforce and Lord Simon of Glaisdale, dissenting but on other grounds. The statement by Holmes J., accepted also by the majority of the Privy Council, was made in Fairbanks v. Snow 13 N.E. 596, 598 (1887).

contracts.[1] The courts held that where a party had made a payment in consequence of such coercion he could recover the amount by means of the action for money had and received. In Moses v. Macfarlan, Lord Mansfield declared that such an action would lie "for money got through imposition, (express, or implied;) or extortion; or oppression."[2] The fact that executed rather than executory contracts were the rule in the eighteenth century and that the issue of duress arose almost exclusively in respect of claims for the recovery of money paid in consequence of duress of goods or of unlawful demands made by a person or body who was in a monopolistic position, meant that at that time the common law, in effect, recognised economic duress and gave relief where it occurred. The various manifestations of "economic duress" of which the courts took note can be classified as follows:

(a) "Duress of Goods"

The development of the doctrine known as duress of goods - the unlawful detention or threatened detention of goods - began in the early eighteenth century with Astley v. Reynolds.[3] In that case the defendant pledgee refused to deliver plate which was deposited with him as security for a loan unless the plaintiff pledgor paid a sum far in excess of the legal interest on the loan. The court allowed recovery of the surplus over and above the legal rate of interest in an action for money had and received and said:

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1 Atiyah, The Rise and Fall of Freedom of Contract, 434-435.

2 (1760) 2 Burr. 1005, 1012.

3 (1731) 2 Str. 915.

> /T/his is a payment by compulsion; the plaintiff might have such an immediate want of his goods, that an action of trover would not do his business: where the rule volenti non fit iniuria is applied, it must be where the party had his freedom of exercising his will, which this man had not: we must take it he paid the money relying on his legal remedy to get it back again.[1]

The doctrine initiated in Astley v. Reynolds was subsequently confirmed and applied in a number of cases which involved goods as varied as a wagonload of hams,[2] title deeds to property,[3] insurance policies,[4] an aeroplane,[5] and a ship held under lien.[6]

Apart from the fact that the object of duress in these cases related to an economic interest rather than to the person of the threatened party the divergence from traditional doctrine was not as extreme as it would seem at first sight. Not only was the type of duress relatively crude and limited in character, but the association with tort law was retained in that the duress exercised was also independently wrongful. The action for money had and received was thus merely an additional remedy, existing next to the damage remedy already available to the injured party.[7] However, the development of this jurisdiction involved an implicit recognition that the situation where money was paid under duress of goods raised peculiar issues for which a damage remedy based on tort was not always particularly suited.

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1 Ibid., 916.

2 Irving v. Wilson (1791) 4 T.R. 485.

3 Pratt v. Vizard (1833) 5 B. & Ad. 808; Oates v. Hudson (1851) 6 Ex. 346; Fraser v. Pendlebury (1861) 31 L.J.C.P. 1.

4 Shaw v. Woodcock (1827) 7 B. & C. 73.

5 T.D. Keegan Ltd. v. Palmer /1961/ 2 Ll. Rep. 449.

6 Somes v. British Empire Shipping Co. (1860) 9 H.L. Cas.338.

7 See generally Dawson, op. cit.

In order to succeed in an action for money had and received the plaintiff merely had to show that he had paid the money in order to redeem goods which belonged to him or to which he had a right of possession,[1] and which had been illegally detained by the defendant.[2] Although the court in Astley v. Reynolds also referred to the fact that the payment was compelled and that consequently the plaintiff did not have the freedom to exercise his will, the early cases focus almost exclusively on the wrongfulness of the detention and automatically assume that where money had been paid to retrieve goods wrongfully detained such payment would be "involuntary".[3] In addition, no specific degree of coercion had to be proved - it was sufficient if the money had been paid in the circumstances mentioned above. The mere fact that the detention was illegal and the payment so clearly unjust was thought sufficient to dispense with any exhaustive inquiry as to the effect of coercion on the plaintiff.

It was, however, inevitable that with the greater emphasis being placed on the consensual aspects of contracts generally the requirement of "involuntariness", of whether the payment was in fact compelled by the threat, should gain in importance. Proof of involuntariness was necessary in order to distinguish payment made

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1 Fell v. Whittaker (1871) L.R. 7 Q.B. 120.

2 See, for example, Valpy v. Manley (1845) 1 C.B. 594, 603.

3 See, for example, Irving v. Wilson (1791) 4 T.R. 485, 486 per Lord Kenyon C.J.: "/T/he defendants took the money under circumstances which could by no possibility justify them, and therefore this could not be called a voluntary payment"; Shaw v. Woodcock (1827) 7 B. & C. 73, 84; Oates v. Hudson (1851) 6 Ex. 346. "Involuntary payment" here bore a specialised meaning and entailed a showing that the payment was made because of the duress and not willingly in spite of it.

under compulsion from payment made voluntarily as a settlement or a compromise.[1] But again this requirement was liberally interpreted by the courts. The question of involuntariness was closely intertwined with the question of whether a tort remedy would provide sufficient protection. It was far more time consuming to rely on one's tort remedy than it was to pay the amount claimed immediately with the intention of recovering it at a later stage by means of the action for money had and received. Where, therefore, the plaintiff needed his goods urgently it was usually assumed by the court that the slower tort remedy would be an inadequate remedy and, following from that, that the plaintiff had paid involuntarily.[2] Payment under duress could also be inferred from the fact that the plaintiff had paid the amount under protest, while reserving his legal rights.[3] Such protest was not, however, essential to prove that the plaintiff had acted under coercion. On the whole, there was little inquiry into the probable effect on the plaintiff of not getting his goods back immediately. It was mostly taken for granted that he would suffer economic injury and thus that the exercise of coercion had left him with no choice but to comply with the demand made by the coercing party.[4] It was thus clear that duress of goods, far from remaining a mere alternative remedy, was gaining a wider application

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1 See as to the meaning of a "compromise" Mason v. The State of New South Wales (1959) 102 C.L.R. 108, 143.

2 See, for example, the Pigott case cited in Cartwright v. Rowley (1799) 2 Esp. 723; Valpy v. Manley (1845) 1 C.B. 594, 603; Ashmole v. Wainwright (1842) 2 Q.B. 837.

3 Maskell v. Horner [1915] 3 K.B. 106, 120-121.

4 Dawson op. cit., 257-258.

and greater independence. "Relatively narrow, but within its limits distinctly favorable to relief, the law of 'duress of goods' provides the starting point, the central type-case, of economic duress."[1]

Although it was thus a well established principle that payment made under duress of goods could be recovered, the case of Skeate v. Beale[2] is usually cited as authority for the proposition that duress of goods does not affect the validity of an agreement to pay money, because in terms of the common law doctrine only duress of person could serve as a defence to a contract. The refusal to assign an invalidating effect to duress of goods could be explained by the fact that the nineteenth century courts applied, without modification, principles which had been developed in respect of executed contracts to executory contracts.[3]

But a more fundamental reason for the reluctance of the common law to extend the scope of duress beyond threats to the person by also taking account of the variety of economic pressures which could be exerted in order to extract a promise, lay in the classical theory of contract. That theory was firmly rooted in the market economy and it therefore precluded the treatment of economic pressure, which was intrinsic to the market structure, as a factor which vitiated consent.[4] Duress therefore, remained confined to the cruder forms of coercion and the doctrine disregarded the most important manifest-

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1 Ibid., 256.

2 (1841) 11 Ad. & E. 983. Also Sumner v. Ferryman (1708) 11 Mod. 201; Atlee v. Backhouse (1838) 3M.& W. 633. Cf. J. Beatson, Duress as a Vitiating Factor in Contract (1974) C.L.J. 97.

3 Atiyah, op. cit., 434-436.

4 Ibid., 436; Dawson op. cit., 266.

ation of coercion in the market economy, economic pressure. And because the legitimation of economic pressure largely obviated the need to resort to duress of the person as a means of procuring a promise, the common law doctrine of duress lost most of its relevance.

The paradoxical rule in Skeate v. Beale, although never accepted without criticism,[1] was instrumental in delaying for more than a century the development of a coherent doctrine of economic duress. However, in the recent case of The Siboen and the Sibotre,[2] Kerr J. criticised the authority of Skeate v. Beale[3] and declared that in his opinion English law was not as limited as this and that "the true question is ultimately whether or not the agreement in question is to be regarded as having been concluded voluntarily."[4] In the subsequent case of The Atlantic Baron,[5] Mocatta J. quoted with approval Kerr J.'s criticism of the so-called rule in Skeate v. Beale and maintained that where "economic duress" led to a contract for consideration such a contract was voidable.[6] In Pao On v. Lau Yiu[7] the Privy Council seems to have held the view that the rule in Skeate v. Beale was good law, but that there was nothing contrary

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1 Hills v. Street (1828) 5 Bing. 37 and Tamvaco v. Simpson (1866) L.R.1 C.P. 363 provided some evidence for the proposition that money paid under a contract might be recovered.

2 [1976] 1 Ll. Rep. 293, discussed by Beatson (1976) 92 L.Q.R.496.

3 Kerr J. apparently accepted the suggestion that the dictum in which Lord Denman set out the so-called rule of Skeate v. Beale was obiter. Lord Denman himself referred in Wakefield v. Newton (1844) 6 Q.B. 276 to cases such as Skeate v. Beale as "that class where the parties have come to a voluntary settlement of their concerns, and have chosen to pay what is found due."

4 Ibid., 335.

5 North Ocean Shipping Co.Ltd. v. Hyundai Construction Co. Ltd. [1978] 3 All E.R.1170, discussed by J. Adams (1979) 42 Mod.L.Rev. 557.

6 Ibid., 1182.

7 [1979] 3 All E.R. 65, 79.

to principle in now recognising economic duress as a factor which could render a contract voidable.

As a result of the restrictive effect of Skeate v. Beale the courts have been compelled to approach the problem of economic coercion in a roundabout way through the doctrine of consideration. It has been said that if in return for a variation in the existing contract, the party who desired it, undertook to perform no more than what he already owed under the contract there would be no consideration to support the new contract.[1] In D. & C. Builders v. Rees,[2] for example, Lord Denning M.R. and Danckwerts L.J. held that a settlement of a claim made under economic pressure was invalid because it was not supported by consideration or, alternatively, that there was no true accord because "no person can insist on a settlement procured by intimidation."[3] Reviewing that case in The Siboen and the Sibotre, Kerr J. explained the judgment as being based on duress and declared that it would have been no different had there been nominal but legally sufficient consideration.[4] This is a highly commendable approach: despite the fact that the courts in the process of finding consideration or not have probably been greatly influenced by the fairness of the modifying agreement,[5] the pre-existing duty rule, as this technique was sometimes called, might ultimately operate arbitrarily and was thus an unsuitable instrument with which to combat unfair agreements

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1 Stilk v. Myrick (1809) 2 Camp. 317.

2 [1966] 2 Q.B.617, discussed by W.R. Cornish in (1966) 29 Mod.L.Rev.428.

3 Ibid., 625 per Lord Denning M.R.

4 [1976] 1 Ll.Rep.293, 336.

5 Adams, op. cit., 559.

exacted under economic coercion.

The question of whether a promise to perform or the performance of a pre-existing contractual obligation could be valid consideration for an agreement was extensively discussed and answered in the affirmative in Pao On v. Lau Yiu.[1] Nevertheless, the Board was of the opinion that such a contract could still be avoided if it was procured by economic duress. It refused, however, to entertain the idea that in the absence of duress, public policy could invalidate that consideration if there had been a threat to repudiate a pre-existing contractual duty or unfair use of a dominant bargaining position.

(b) Unlawful threats by a person or body in a monopolistic position

Towards the middle of the nineteenth century a different line of cases began to appear concerning excessive demands made by a person or body who is in a monopolistic position and where the plaintiff complied with the demand because he was unable to satisfy his needs elsewhere.[2] The most important examples were provided by overcharges by common carriers.[3] From the earliest stage this jurisdiction tended to overlap with the duress of goods cases as the demand for an excessive freight rate often occurred at a time when the plaintiff's goods were already in the possession of the carrier.[4]

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1 [1979] 3 All E.R.65, 76-78. See also the discussion of the rule by Mocatta J. in The Atlantic Baron [1978] 3 All E.R.1170.

2 Goff and Jones, op. cit., 174.

3 The first case was Parker v. Great Western Railway Co. (1844) 7 M.& G. 253, in which the court ordered repayment of the excess freight charges which had been collected by the company. In that case there was no duress of goods, but in Ashmole v. Wainwright (1842) 2 Q.B. 837 a carrier who had refused to deliver goods until excessive charges had been paid was ordered to repay such excess to the plaintiff.

4 Dawson, op. cit., 258.

Just as in the previous ventures into the sphere of economic duress, the courts' foray into this particular field did not involve a major movement in policy, for the common law had already enforced upon the common carrier an obligation

> to accept and carry all goods delivered to him for carriage according to his profession (unless he had some reasonable excuse for not doing so) on being paid a reasonable compensation for so doing; and if the carrier refused to accept such goods, an action lay against him for so refusing; and if the customer, in order to induce the carrier to perform his duty, paid, under protest, a larger sum than was reasonable, he might recover back the surplus beyond what the carrier was entitled to receive in an action for money had and received as being money extorted from him.[1]

Although the plaintiff generally paid the charges demanded under protest this was not a necessary requirement.[2] Instead, the courts emphasized the inequality of the parties and, drawing on the analogy of the colore officii cases, inferred from the fact that the plaintiff was, vis-à-vis the monopolistic carrier, in an inferior bargaining position, that the payment was made as a result of coercion.[3] The inference that payment was made "involuntarily" was further strengthened by the circumstance that the plaintiff's economic existence may have depended upon using the facilities of the carriers, and as the latter were frequently monopolies the plaintiff had no choice but to submit to the demands.[4] Involuntariness could be inferred even where it was merely a commercial necessity that the plaintiff use the carriers.

In the United States this jurisdiction has been expanded to

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1 Great Western Railway v. Sutton (1868-1869) L.R. 4 H.L.226, 237 per Blackburn J.

2 J. Dalzell, Duress by Economic Pressure I (1942) 20 N.C.L. Rev. 237, 244.

3 Dawson op. cit., 259; Dalzell op. cit., 244-246.

4 Dawson, op. cit., 260; Dalzell, op. cit., 244-246.

include unlawful threats made by all public utility companies. Both Dawson[1] and Dalzell[2] referred to many cases in which the courts have held that where a public utility company threatened to withhold the supply of gas, water or electricity or other service unless an excessive payment was made and the plaintiff, compelled by immediate commercial needs, met this demand, then such excess was recoverable as having been paid under compulsion in the legal sense. The payment by the plaintiff was held to be involuntary on the following considerations:

> To make the payment a voluntary one, the parties should stand upon an equal footing ... But where one has the advantage of the other, where delay or a resort to the law is indifferent to the one but may produce serious loss and injury to the other, it is unconscionable to press such advantage to the obtaining of unjust demands. That is extortion.[3]

A similar principle was applied in South of Scotland Electricity Board v. British Oxygen Co. Ltd.[4] where the respondents were supplied with high voltage electricity by the appellants. As electricity at high voltage was cheaper to produce than at low voltage the respondents were charged at a lower tariff level than consumers of low voltage electricity. Nevertheless, the respondents complained that despite the different tariffs the differential between them was insufficient to reflect the difference in production cost between high and low voltage electricity, and that there was therefore "undue

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1 Dawson, op. cit., 259.

2 Dalzell, op. cit., 243-246.

3 Beckwith v. Guy Frisbie & Sons, 32 Vt. 559 (1860) as cited by Dalzell, op. cit., 245.

4 [1959] 1 W.L.R. 587.

discrimination" against consumers in the position of the respondents. Such discrimination, the respondents averred, was contrary to statute.[1] Respondents also claimed restitution of the "overcharges" made by them. The House of Lords, affirming the decision of the Court of Session[2], held that there should be proof before answer as far as the averments of "undue discrimination" was concerned, because such discrimination could exist even though the respondents were charged a lower tariff than consumers of low voltage electricity. In deciding whether there was such discrimination the cost of producing high voltage electricity was a relevant consideration. In the opinion of the House an action for restitution of the overcharges would be available if undue discrimination was proved. In support of this view Lord Merriman cited[3] the following dictum by Willes J. in Great Western Railway Co. v. Sutton:[4]

> /W/hen a man pays more than he is bound to do by law for the performance of a duty which the law says is owed to him for nothing, or for less than he has paid, there is a compulsion or concussion in respect of which he is entitled to recover the excess by condictio indebiti, or action for money had and received.

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1 Electricity Act 1947, section 37(8); Hydro Electric Development (Scotland) Act 1943, section 10A(5).

2 1958 S.C. 53.

3 /1959/ 1 W.L.R. 587, 607.

4 (1868-1869) L.R. 4 H.L. 226, 249.

This survey shows that the requirements for the recovery of money paid under duress of goods or in order to obtain the performance of a duty, were much less stringent than those which governed traditional common law duress. In particular, the courts have been very ready to accept the coercive qualities of the threats made and thus to draw the conclusion that the money was paid "involuntarily". The exaction by those types of coercion of money which was clearly not due made those transactions obviously unfair and at least one commentator has remarked that the severity of the duress rules might differ according to the fairness of the resulting transaction.[1]

The value of these modest judicial sorties into the sphere of economic duress lay not so much in the new types of coercion which the courts regarded as relevant - they were relatively unsophisticated - but in the general recognition by the courts that economic pressure could be as coercive as duress of the person. The steps taken in The Siboen and the Sibotre[2] and subsequent cases towards the regulation of those economic pressures which lawyers had until recently regarded as essential concomitants of the economic structure in which contract law is so firmly rooted was directly traceable to the "duress of goods" and related cases. The question which now arises is the extent to which economic pressure has been recognised as either affecting the validity of a contract or as a ground for the recovery of benefits conferred as a result of such pressure.

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1 R.J. Sutton, Duress by Threatened Breach of Contract (1974) 20 McG. L.J. 554, 560.

2 [1976] 1 Ll. Rep. 293.

Economic duress in modern law

As Dalzell[1] indicated, economic pressure can take many forms. Apart from the manifestations discussed before, there have been a few isolated cases in which a threat to break a contract was recognised as legally relevant. In Close v. Phipps[2] the attorney of a mortgagee threatened to sell the mortgaged property unless his demand that he be paid an amount additional to the mortgage sum was met. The money, which was not due, was paid under protest and afterwards recovered in an action for money had and received. In The Atlantic Baron,[3] Mocatta J. accepted that the payment in Close v. Phipps was made under duress, the duress being a threatened breach of contract. In the Chancery case of Ormes v. Beadel,[4] a builder entered into a contract with a debtor under threat that unless he did so the latter would not pay his debts. The debtor knew that the builder needed the money urgently to pay his employees who had said that they would otherwise stop work. Stuart V.C. set aside the agreement and said:

> Where an agreement hard and inequitable in itself, has been exacted under circumstances of pressure on the part of the person who exacts it, this court will set it aside.[5]

A long time was to pass before an English court was again called upon to decide whether a threat to breach a contract constituted illegitimate coercion.

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1 Op. cit.

2 (1844) 7 M. & G. 586.

3 [1978] 3 All E.R. 1170, 1178.

4 (1860) 2 Giff. 166, reversed on a different ground in (1860) 2 De G.F. & J. 333.

5 Ibid., 174.

In The Siboen and the Sibotre[1] two ships were time chartered at a rate of 4.40 dollars per ton per month. The market subsequently slumped and the cost of a charter went down to 2.80 dollars. The charterers, desirous of getting a better deal for themselves asked for a renegotiation of the rate. This was refused. The charterers and their parent company then fraudulently represented that they had no assets and would go bankrupt if the rate was not renegotiated. They also threatened to repudiate the contract unless this was done. The owners who had mortgaged the ships and used the charter income to repay the mortgage feared that unless they renogiated they would lose the charter with the result that the ships would be unused because of the slump. They therefore succumbed to the threat. Before the court, counsel for the owners argued that the renegotiation was voidable for duress and submitted that the

> defence of duress is made out whenever one party to a contract threatens [whether in good faith or not] to commit a breach of it and the other party agrees to vary or cancel the contract under this threat because it has no effective legal remedy in respect of the threatened breach ... [D]uress must a fortiori be a defence when the party threatening to break the contract is putting forward some justification for doing so without any bona fides.[2]

Kerr J. thought that this contention was "much too wide",[3] apparently because it implied that even a settlement concluded "voluntarily" in spite of a threat, could afterwards be avoided on the ground of duress.

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1 [1976] 1 Ll.Rep. 293.

2 Ibid., 334-335.

3 Ibid., 335.

Yet he did say that a plea of "coercion or compulsion" would be available to a party who had entered into a contract under the imminent threat of having his house burnt down or a valuable picture slashed[1] and he acknowledged the strong authority of Australian cases such as T.A. Sundell & Sons Pty. Ltd. v. Emm Yannoulatos (Overseas) Pty.Ltd.[2] in which the court accepted that "a compulsive threat ... to refrain from performing merely a contractual duty"[3] could constitute legal duress.

> The true question, Kerr J. maintained, was
>
> whether or not the agreement in question is to be regarded as having been concluded voluntarily ... /T/he Court must in every case at least be satisfied that the consent of the other party was overborne by compulsion so as to deprive him of any animus contrahendi.[4]

Kerr J. did not feel that in the present case the owners had contracted involuntarily. There was no protest by the owners, and later they sought to uphold the renegotiated charter by arbitration. The owner was "acting under great pressure, but only commercial pressure, and not under anything which could, in law, be regarded as a coercion of his will so as to vitiate his consent."[5] In view of the fact that protest is not the only way of showing that a contract was concluded "involuntarily" this conclusion is open to question, especially because of the charterers' fraudulent representation that they had no assets and the implication from that that an action for damages because of breach of contract would bring but cold comfort to the owners, rendered the

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1 Ibid.

2 /1956/ S.R. (N.S.W.) 323.

3 Ibid., 328.

4 /1976/ 1 Ll.Rep. 293, 335 and 336.

5 Ibid., 336.

"commercial pressure" sufficiently coercive to constitute legal duress.

In The Atlantic Baron,[1] shipbuilders contracted to build a tanker for a shipping company at a price fixed in U.S. dollars. In consequence of a devaluation of the U.S. dollar the builders, without legal justification, demanded an increase of 10 per cent on the balance of the purchase price. The buyers rejected the demand but subsequently concluded an advantageous contract for the charter of the tanker and as the builder had by then threatened to terminate the contract unless the additional payment was made, the buyers agreed "without prejudice to our rights" to pay the sum. The buyers later instituted an action for recovery of the additional payment, inter alia on the ground of duress. Mocatta J. accepted that the agreement was concluded under duress but held that the buyers could not recover the additional sum because they had subsequently affirmed the agreement.

In holding that the threat by the builders constituted relievable duress Mocatta J. accepted as authority a dictum of Isaacs J. in Smith v. William Charlick Ltd.[2] to the effect that "compulsion" includes every species of duress or conduct analogous to duress. "Compulsion", according to Mocatta J., therefore could take the form of economic pressure and a threat to break a contract could amount to economic duress.[3]

In Pao On v. Lau Yiu,[4] the plaintiffs contracted to sell to a public company in which the defendants had the majority shareholding

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1 [1978] 3 All E.R. 1170.
2 (1924) 34 C.L.R. 38, 56.
3 [1978] 3 All E.R. 1170, 1182.
4 [1979] 3 All E.R. 65.

the shares of a private company whose only asset was a building. In terms of the contract the plaintiffs were to be paid by the allotment to them of shares in the public company. As the defendants were afraid that sudden heavy selling of shares in their company might depress the market and thus lead to a devaluation of their shareholding, the plaintiffs had to undertake not to sell a portion of the shares allotted to them for a certain time. The defendants, in order to protect the plaintiffs against a drop in the value of their shares during this period of postponement, agreed to buy back the shares at the price which, for the purposes of the sale, they were deemed to have. The plaintiffs suddenly realized that they had made a bad bargain, because if the value of the shares which they were allotted rose in value they were still bound to sell them to the defendants at their original deemed value. The plaintiffs, therefore, threatened not to complete the transaction unless the parties agreed on a proper indemnity. The defendants were aware that they could claim specific performance, but for commercial reasons decided to comply with the plaintiffs' demand. The value of the shares in the defendants' company subsequently fell dramatically and the plaintiffs instituted an action for the sum which was owed to them in terms of the indemnity. The defendants' defence was inter alia that the indemnity had been induced by economic duress and was thus voidable.

On the facts the Privy Council had no difficulty in rejecting that proposition. Although it agreed that commercial pressure might constitute duress that was not in itself sufficient to render the contract voidable. The commercial pressure had to be such that "the victim's consent to the contract was not a voluntary act on his part."[1]

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[1] Ibid., 79.

From the cases examined it appears that commercial pressure, either as a result of a threat by the defendant not to perform his contractual obligations if his demand was not met[1] or through a threat by him to cancel a contract if the plaintiff did not succumb to his demands,[2] might constitute legal duress. However, it will be illegitimate pressure and thus duress only when the pressure is such that it coerces the will of the plaintiff so as to vitiate his consent.[3]

In all three cases examined the parties had threatened to do something which would have been unlawful. Yet, in none of the judgments was it stated to be a requirement that the threat had to be illegitimate in order to amount to relievable duress. The impression is generally created that it is the coerciveness of the threat which renders it wrongful and not which kind of threat it was. Kerr J. even quoted with apparent approval the rhetorical question of Collins M.R. in Kaufman v. Gerson, "/W/hat does it matter what particular form of coercion is used, so long as the will is coerced?"[4] If indeed the position taken by the courts was that the threat itself need not be wrongful it would seem to conflict with the dicta in Barton v. Armstrong[5] in which two steps were proposed where duress was alleged:

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1 The Atlantic Baron /1978/ 3 All E.R. 1170; Pao On v. Lau Yiu /1979/ 3 All E.R. 65.

2 The Siboen and the Sibotre /1976/ 1 Ll. Rep. 293; D. & C. Builders v. Rees /1966/ 2 Q.B. 617.

3 See, for example, Pao On v. Lau Yiu /1979/3 All E.R. 65, 78.

4 (1904) 1 K.B. 591, 597, as cited in The Siboen and the Sibotre /1976/ 1 Ll. Rep. 293, 335.

5 /1976/ A.C. 104, 121 per Lord Wilberforce and Lord Simon, dissenting, but on other grounds.

firstly, to determine whether some illegitimate means of persuasion had been used, and secondly, to establish the relationship between the illegitimate means used and the action taken by the party at whom the threat was directed.

A test of duress based exclusively on the coerciveness of the threat holds potentially important implications for the validity of all agreements induced by economic pressure, especially in view of the fact that economic pressure of greater or lesser intensity is an inherent feature of market economies. Does such a formulation of duress mean that a party may be freed from his contractual obligations merely because he had to deal with a particular person or company in the absence of anybody else supplying a particular commodity? English law has as yet been unwilling to give relief solely on that ground,[1] although it has allowed the scrutiny of some standard form contracts to determine whether their terms were fair.[2]

Commonwealth authorities have taken the view that duress can only be found where a threat was wrongful. In Smith v. William Charlick Ltd.[3] for example, the respondents were wheat dealers who bought their produce from the Australian Wheat Board. After allowing an increase in the price of wheat the Board discovered that the respondents had profited greatly by selling the old, cheaper produce at the new higher prices and demanded from them a sum of money. In

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1 Eric Gnapp Ltd. v. Petroleum Board [1949] 1 All E.R. 980.

2 A Schroeder Music Publishing Co. Ltd. v. Macaulay [1974] 1 W.L.R. 1308, 1315-1316 per Lord Diplock.

3 (1924) 34 C.L.R. 38. See also Morton Construction Co. v. City of Hamilton (1961) 31 D.L.R. (2d) 323.

addition, the Board threatened that unless their demand was met they would not deal with the respondents in future. Since the Board was the monopoly supplier the respondents had no choice but to comply. Yet the High Court of Australia dismissed respondents' claim for the recovery of the sum paid on the ground that the Board's threat was not wrongful. The money was paid "not in order to have that done which the Board was legally bound to do, but in order to induce the Board to do that which it was under no legal obligation to do."[1]

Nevertheless, a case can be made out for the proposition that in the context of duress "wrongfulness" should not be defined by reference only to whether a threat is actionable or not. The equitable doctrine of pressure has already provided some authority for the view that pressure which was otherwise lawful might be wrongful if it is used merely to induce a person to enter into a contract. A similar approach can be found in some American cases. In discussing the requirement of wrongfulness the New Jersey Supreme Court said in Rubinstein v. Rubinstein that

> ... means in themselves lawful must not be so oppressively used as to constitute, e.g., an abuse of legal remedies... The act or conduct complained of need not be "unlawful" in the technical sense of the term; it suffices if it is 'wrongful in sense that it is so oppressive under given circumstances as to constrain one to do what his free will would refuse...'[2]

In a case where the threat is not in itself unlawful the fairness of the resulting contract may be an important consideration in deciding whether the threat was "wrongful" so as to constitute duress.

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1 (1924) 34 C.L.R. 38, 51 per Knox C.J.

2 20 N.J. 359, 367, 120 A. 2d 11, 15 (1956) as cited by Sutton, op. cit., 583.

Nevertheless, a duress test framed solely in terms of the coercive quality of the threat does raise some conceptual problems, especially by its excessive emphasis on the requirement that the threatened party's will must be overborne by the pressure. It has long been pointed out that duress, although it restricts a person's choice, does not necessarily exclude volition, and conversely, that the mere fact that relievable duress has not been found does not mean that a party concluded a contract uninduced by any pressure.[1] In Lloyds Bank Ltd. v. Bundy[2] Lord Denning M.R. indicated, quite correctly in my view, that " one who is in extreme need may knowingly consent to a most improvident bargain, solely to relieve the straits in which he finds himself"[3], and he thus "avoided any reference to the will of the one being 'dominated' or 'overcome' by the other."[4] Holmes J. similarly recognised the reality of the situation when he said:

> It is always for the interest of a party under duress to choose the lesser of two evils. But the fact that a choice was made according to interest does not exclude duress. It is the characteristic of duress properly so called.[5]

In view of these difficulties it would be better to require firstly, and before any attempt is made at establishing a causal link between the pressure exerted and the subsequent action of the pressurised party, that the threat was "wrongful" even if the term is then

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1 See for example, Dalzell, op. cit., 238-240; R.L. Hale, Bargaining, Duress and Economic Liberty (1943) 43 Col.L.Rev. 603, 615-618; Atiyah, op. cit., 436; Dawson, op. cit., 266-267.

2 [1975] 1 Q.B. 326.

3 Ibid., 339.

4 Ibid.

5 Union Pacific Railway Co. v. Public Service Commission of Missouri, 248 U.S. 67, 70 (1918).

used to include conduct which, although not unlawful, violates the community's standards of fair conduct. If such a proposition is accepted then the primary task of the courts will not be merely to establish whether a threat coerced the will of the threatened party so as to vitiate his consent, but to delimit the kinds of pressure which are wrongful and may thus lead to a finding of duress.

> In establishing whether there was
>
> a coercion of will such that there was no true consent, it is material to enquire whether the person alleged to have been coerced did or did not protest; whether, at the time he was allegedly coerced into making the contract, he did or did not have an alternative course open to him such as an adequate legal remedy; whether he was independently advised; and whether after entering the contract he took steps to avoid it.[1]

The test used to determine whether a party's will was coerced by a threat is subjective and the court is therefore permitted to take into account any peculiar circumstances such as economic necessity or his mental state which might have affected him in deciding whether or not to meet the threatening party's demands. Such an approach has been followed in the duress of goods cases as well as in equity's doctrine of pressure and it would seem from The Atlantic Baron that it has been adopted in the sphere of economic duress as well. In that case Mocatta J. inferred "involuntariness" from the fact that, in view of their advantageous chartering agreement, it would have been "unreasonable" to expect of the owners to have taken the alternative course of arbitration.[2] This was done despite the fact that the coercing

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[1] Pao On v. Lau Yiu /1979/ 3 All E.R. 65, 78.

[2] /1978/ 3 All E.R. 1170, 1182-1183.

party was unaware of the conclusion of the chartering agreement. However, if he had been aware of, and had specifically taken advantage of, his counterparty's difficulties to extort an unreasonable benefit there should be little to prevent the court from holding that the threatened party had conferred the benefit "involuntarily". In such a case the dividing line between economic duress and equitable fraud is very thin and it is clear from the study of economic duress made by Dalzell that if duress is given a wide definition, many of the cases which in this study have been dealt with under equitable fraud can also be explained on the basis of economic duress.

The relationship between duress and substantive fairness

In modern law, duress is generally portrayed as relating to the quality of a person's assent to a contract. This has not always been the case and in 1790 Powell[1] also postulated substantive unfairness as a reason for avoiding a contract entered into under duress. Nevertheless, it is clear that relievable duress may be found irrespective of whether the contract was fair or not and in transactions where no economic elements are involved the question of substantive unfairness will not arise.

Yet there is a close, but usually unexpressed, relation between the doctrine of duress and the objective merits of the contract.[2] Duress, as well as the equitable doctrine of pressure, are normally used to avoid acts by one person - payments or transfers, the assumption

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1 Essay on the Law of Contracts and Agreements, 160-161.

2 See Hale, op. cit., 621-625; Dawson, op. cit., 282-288.

or release of debts - for which no or an unequal return was given.[1] In addition, the cases indicate that recovery of money paid under duress is usually limited to the amount which was not due. The objective merits of a contract may also influence the requirements which are set for a finding of duress, the strictness with which these requirements are enforced, and the extension of the doctrine of duress. Where the threats used to induce a contract are less overtly wrongful, such as in the developing area of economic duress, the unfairness of the contract may influence the court in finding that the threat amounted to legal duress.

Dawson has contended that the real question in respect of economic duress is not the wrongfulness of the coercion, but the unequal exchange and whether it resulted from an unconscionable use of economic power.[2] Although there is no doubt that even American courts have not gone this far[3] there are signs that English courts are increasingly willing to use economic duress as a means of dealing with unfair contracts arising from the use of economic pressure.

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1 J.P. Dawson, Unconscionable Coercion: The German Version (1976) 89 Harv.L.Rev. 1041, 1048.

2 Economic Duress - An Essay in Perspective (1945) 47 Mich.L.Rev. 253, 287.

3 Section 318 of the Restatement of Contracts 2d, Tentative Draft (1977) now provides for much greater emphasis on the fairness of contract terms exacted under threat in deciding whether relief should be given or not.

6 - UNFAIR CONTRACTS IN ADMIRALTY[1]

It has been firmly established that salvage agreements may be set aside if their terms are unfair. In Akerblom v. Price, Potter, Walker & Co. Brett L.J. expressed the principle as follows:

> The fundamental rule of administration of maritime law in all courts of maritime jurisdiction is that, whenever the court is called upon to decide between contending parties, upon claims arising with regard to the infinite number of marine casualties, which are generally of so urgent a character that the parties cannot be truly said to be on equal terms as to any agreement they may make with regard to them, the Court will try to discover what in the widest sense of the terms is under the particular circumstances of the particular case fair and just between the parties. If the parties have made no agreement, the Court will decide primarily what is fair and just... If the parties have made an agreement, the Court will enforce it, unless it be manifestly unfair and unjust; but if it be manifestly unfair and unjust, the Court will disregard it and decree what is fair and just.[2]

In determining whether a salvage agreement is fair or not the courts look not only at whether the salvage remuneration is exorbitant or inadequate, but also at the relative positions of the parties at the time of the conclusion of the contract. The courts have recognised that salvage agreements are often concluded at a time when the circumstances of one party are such that he is more or less compelled to accept any terms which the other might wish to impose upon him.[3] The conduct of the salvor and the surrounding circumstances will thus be material factors in deciding on the validity of the salvage agreement.

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1 See generally Kennedy, Civil Salvage, 309-321.

2 (1881) 7 Q.B.D. 129, 132-133.

3 The Mark Lane (1890) 15 P.D. 135; The Port Caledonia and the Anna [1903] P. 184.

Where the demands of the salvor have been unfair the court will set the agreement aside despite the fact that the degree of compulsion would not have been sufficient to invalidate an agreement at common law.[1]

Salvage agreements have generally been set aside because the remuneration stipulated was exorbitant, but the courts have held that a stipulation prescribing a grossly inadequate remuneration might meet the same fate.[2] Whether the remuneration is exorbitant or inadequate is determined by comparing it to the nature and value of the services rendered by the salvor.[3]

Although the courts may set aside a contract solely because of a grossly unfair salvage award,[4] they will generally not interfere where the agreement is equitable except for the fact that the salvage remuneration is more or less than they would have awarded had there been no contract.

The power to strike down unfair salvage agreements rests not only in the English courts, but also in the Court of Session, which, by virtue of the Court of Session Act 1830[5] took over the jurisdiction of the old Scottish Court of Admiralty.

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1 The Mark Lane (1890) 15 P.D. 135, 137.

2 The Phantom (1866) L.R. 1 A. & E. 58.

3 Kennedy, op. cit., 310.

4 Ibid., 313-314.

5 Sections 21-22.

B - SCOTS LAW

1 - USURY AND INEQUALITY OF EXCHANGE

Although the absolute medieval prohibition of usury also operated in Scotland, the taking of interest on money loans became lawful in the late sixteenth century, provided that the rate of interest did not exceed a statutory maximum. Between 1587, the date of the first important Act which allowed the taking of interest,[1] and 1854, when all usury laws were abolished,[2] the statutory maximum fluctuated between 10 and 5 per cent per year.[3] Usury was defined widely in these statutes and generally included interest received through annualrents prior to the term of payment or through the use of wadsets.[4]

In England the concept of usury had an effect far outside the immediate scope of the usury laws. The standard of substantive fairness which the usury laws set and the considerations of protecting the weak and financially embarrassed from exploitation, which underlay them, were important factors in the development of Chancery's doctrines against forfeitures, penalties and equitable fraud. Whether the concept of usury ever gained such a wider significance in Scots law is doubtful.

There were a few early cases in which the courts intervened, apparently because they regarded the transactions in question as contrary to the spirit of the usury laws. In Sutherland v. Sinclair,[5]

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1 1587 c.35.

2 17 & 18 Vict. c.90.

3 See, for example, 1587 c.35, 1633 c.21 and 12 Anne 1713 Stat. 2 c.16.

4 Mackenzie, Laws and Customes of Scotland, in Matters Criminal, 236-247.

5 1696 Mor. 9460. See also Abercrombie v. Earl of Peterborough 1745 Mor. 4894; Borthwick v. Ramsay 1697 Mor. 4981.

for example, an assignation of a tack, granted at the same time as a bond for borrowed money, was not labelled as direct usury

> yet /the Lords/ reduced it as null, being of the same date with the bond for borrowed money, and acknowledged in his oath to have had no other onerous cause but a gratuity.[1]

According to the reporter the Lords had been very severe on this point and he referred to Nisbet v. Humbie[2] "where they would not so much as allow creditors to take gifts from their debtors, else this crime of usury might be under such pretences easily evacuated and eluded".[3] In King v. Ker,[4] where a cautioner claimed a certain sum for his services the defender argued that such payment would amount to an evasion of the usury laws and maintained that the purpose of these laws was "to pull poor debtors out of the claws of such cormorant harpies, and to secure them, that it shall not be in their power to injure themselves by borrowing money at exorbitant rates".[5] The Lords apparently agreed that the cautioner's claim amounted to indirect usury, because they declared the bond, in terms of which he was making the claim, to be contra bonos mores and reduced it. Kames, reviewing this and some other cases, maintained that they supported the principle that "every benefit taken indirectly by a creditor, for the granting of which no impulsive cause appears but the money lent, will be voided as extorted".[6]

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1 Ibid.

2 1677 Mor. 9459.

3 1696 Mor. 9460.

4 1711 Mor. 9461.

5 Ibid. 9463.

6 Equity, 69.

In more modern law there are two cases concerning moneylending where the courts gave relief, apparently on the sole basis that the interest rates charged were colossal. In Young v. Gordon,[1] an unmarried woman borrowed £104 and gave the moneylender promissory notes to the value of £124. When a month later, Young was unsuccessfully called upon to honour the promissory notes, she was induced to give three more notes to a total value of £250 in exchange for twenty-four hours delay. A few days after the expiry of the final date Gordon claimed £200. The court suspended the charge and limited Young's obligation to the principal sum plus reasonable interest. It described the transaction as most "iniquitous", but was otherwise not very forthcoming as to the grounds for the decision.[2] In the subsequent case of Gordon (Gordon's Administrator) v. Stephen,[3] the defender was an old, simple and timid man who had given bills totalling £198 to the moneylender, but received only £25 in return. Lord Kincairney called the transaction "scandalously extortionate and extravagant"[4] and refused to enforce it, claiming as authority the earlier case of Young v. Gordon and the power of the courts to modify penalties which would otherwise "produce gross injustice". The reference to penalties, which, if exorbitant, were originally modified on the ground of usury,[5]

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1 (1896) 23 R. 419.

2 Gloag on Contract, 492 suggests that the judgment was based on fraud which was inferred from the gross inadequacy of consideration.

3 1902 9 S.L.T. 397.

4 Ibid., 398.

5 Ante, 40.

might be taken to mean that the court, in refusing enforcement, was similarly motivated by considerations of usury. On the other hand, the Moneylender Act 1900, which conferred on the court the power to adjust "harsh and unconscionable" moneylending transactions[1] had then just been passed and although it did not apply to the transactions in question, it is at least probable that the court was influenced by it. In addition, it was clear that the lesion did not stand alone - not only was it explicitly stated in the latter case that Stephen was old, simple and timid, but the enormity of the lesion in the earlier case might also be taken as evidence that Young was either extremely necessitous or, at least, very inexperienced in financial matters.

Apart from these cases there is little evidence to indicate that the concept of usury was given a wider role in Scots law. Both the courts[2] and the institutional writers proved unwilling to advocate relief from a contract merely because there had been inequality in the exchange between the parties. Stair, while conceding that the purpose of the contracting parties was to "keep an equality in the worth and value of the things, fruit, or works interchanged"[3] and that "unjust balances are an abomination to the Lord",[4] rejected the civilian doctrine of laesio enormis,[5] and the notion that an unequal bargain

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1 Section 1.

2 Moneymusk v. Lesley 1635 Mor. 4956; McLachlan v. Watson (1874) S.L.R. 549, 550 and 551; McKirdy v. Anstruther (1839) 1 D. 855, 863; Caledonian Railway Co. v. North British Railway Co. (1881) 8 R. (H.L.) 23, 31; A.B. v. Joel (1849) 12D. 188.

3 I, 10, 14.

4 I, 10, 15.

5 I, 10, 14 citing Fairie v. Inglis 1669 Mor. 14231. See also Kames, op.cit., 80; Erskine IV, 1, 27; Bell, Commentaries, I. 317.

should ex post facto lead to reparation, on the ground that as the value of goods depended upon "necessity, utility and delectation"[1] it was not static and might change along with changing circumstances. There could thus be no determinant of the value of goods other than the free parties themselves. However, according to Stair an equality had to be observed in respect of penalties and irritancies.[2]

Scots law made one exception to the general principle that inequality in the bargain was an insufficient ground for reduction. A contract concluded by a minor was and still is, reducible at any time within four years after he has reached majority, upon proof of minority and great lesion.[3] The requirement of enorm lesion will be met if it is shown that there was a striking disproportion between the values exchanged.[4] In general, the burden of proving lesion is on the minor,[5] but lesion will be presumed where he made a donation or gratuitously gave up his rights.[6] Lesion will furthermore be presumed where a minor has squandered the price paid for a sale made by him or a loan made to him.[7]

Apart from a few exceptional cases Scots law has been unwilling to grant relief from unfair bargains by analogy to the usury laws or on the sole ground of lesion: "For though a wise man would not have

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1 I, 10, 14.

2 Ibid.

3 Stair I, 6, 44; Erskine I, 7, 34; McGuire v. Addie & Sons' Collieries 1950 S.C. 537.

4 Robertson v. Henderson (1905) 7 F. 776.

5 Falconer v. Thomson 1792 Mor. 16380.

6 Stair I, 6, 44; Erskine I, 7, 37.

7 Ferguson v. Yuill (1835) 13 S. 886.

given such a right, yet the Lords are not curators to all who in this manner dispose upon their rights".[1] Even in the time of Stair[2] it was realized that to relieve from bargains merely because they stipulated for an unequal exchange would be detrimental to commerce. It would, however, be wrong to draw the conclusion that the Scots courts regarded the fairness of contracts as irrelevant to the question of whether or not they should be enforced. The various ways through which the courts have attempted to control unfair contracts will be examined in the following chapters.

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1 Smith v. Napier 1697 Mor. 4955.

2 I, 10, 14.

2- BONA FIDES IN THE LAW OF CONTRACT

Some writers on modern law, notably Professors T.B. Smith[1] and J.J. Gow[2] have expressed the opinion that Scots law recognises a general standard of bona fides in contracts. This view has recently been echoed by the Scottish Law Commission.[3] Gloag, in his treatise on Contract,[4] referred to the fact that contracts are construed on the assumption of honest dealing, but was otherwise silent on the subject. Smith, Gow and the Scottish Law Commission relied almost exclusively on statements by the institutional writers as authority for their views.

The concept of bona fides has played an important role in the "moralization of contracts"[5] in many jurisdictions, notably those of continental Europe[6] and could fulfil a similar function in Scots law.

A large number of rules and principles which govern the law of contract can be ascribed to good faith.[7] These individual elements

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1 Short Commentary on the Law of Scotland, 297-298, 756, 830, 838 et seq.

2 Mercantile and Industrial Law of Scotland, 179 et seq. See also by the same author, Warrandice in Sale of Goods (1963) 8 Jur. Rev. 31, 62-64.

3 Memorandum No. 42: Defective Consent and Consequential Matters, II, 74, 141-143.

4 Contract, 400.

5 Ripert, La Regle Morale Dans les Obligations Civiles, 92-93, as cited by R.A. Newman, The Cleft: The Similarity of Fundamental Doctrines of Law which underlies their Conceptual formulation in different Legal systems (1967) 18 Hastings L.J. 481, 503.

6 See generally Newman, op.cit., 502-506.

7 See R.A. Powell, Good Faith in Contracts (1956) 9 Curr. Leg. Prob. 16.

of good faith have infiltrated into almost every aspect of contract law: the formation and performance of contracts, the raising and resolving of contractual disputes, and the taking of remedial action.[1] However, the aim in this chapter is to determine whether or not Scots law ever imposed an overriding requirement of bona fides in contracts. In order to do so it is necessary first to examine the role of bona fides in Roman law, the system in which the concept of bona fides originated.

Bona fides in Roman law

In Roman law a standard of contractual fairness was implemented through the requirement of bona fides. A distinction was drawn between iudicia stricti iuris and iudicia bonae fidei.[2] In the former category, the iudex was confined to a strict and literal interpretation of the formula and had no discretion to take into account outside factors. The harshness of keeping a debtor bound to his obligations under all circumstances was alleviated by providing him with a defence called the exceptio doli.[3] The exceptio had to be expressly inserted in the formula. It required the iudex to take into consideration, in the

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1 R.S. Summers, "Good Faith" in General Contract Law and the Sales Provisions of the Uniform Commercial Code (1968) 54 Va. L. Rev. 195. See also F. Kessler and E. Fine, Culpa in Contrahendo, Bargaining in Good Faith, and Freedom of Contract: A Comparative Study (1964) 77 Harv. L. Rev. 401.

2 See generally Sohm, Institutes of Roman Law, 367-371; Kaser, Roman Private Law, 142 et seq.

3 Sohm, op.cit., 279-282; Kaser, op.cit.; Buckland, A Text-Book of Roman Law, 679.

first place, the fact that the plaintiff had been guilty of dolus, or conscious misrepresentation, at the time of the formation of the contract. However, even where there had been no misrepresentation, the exceptio doli required of the iudex to take account, in the second place, of dolus of which the plaintiff was guilty merely by bringing the action against the debtor.[1] Dolus, in this latter sense, meant that the plaintiff brought the action knowing that it was a violation of bona fides to do so. According to Sohm

> /S/uch would be the case, for example, if a person were to sue on a transaction which he had obtained from the defendant by intimidation, or if he were to sue the defendant in breach of an informal agreement not to sue (pactum de non petendo). In this way the exceptio doli may sometimes serve the purposes of an exceptio metus or exceptio pacti. But Roman jurisprudence did not stop there. An exceptio doli was declared to be available, not only where the plaintiff, by taking legal proceedings, was acting maliciously, but also wherever, as it was said, 'ipsa res in se dolum habet'... i.e. wherever the raising of the action constituted objectively a breach of good faith. The insertion of the exceptio doli in the formula was considered to empower the judge to take account of every single circumstance that would render the condemnation of the defendant substantially unjust... /I/t was this breadth of scope that fitted the exceptio doli for becoming the instrument employed, both in the theory and the practice of Roman law, for effecting such modifications of the material law as equity seemed to require.[2]

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1 Sohm, op.cit., 279-280. Although modern commentators on Roman law sometimes refer to the exceptio doli which pertained to fraudulent misrepresentation as the exceptio doli specialis and to the other as the exceptio doli generalis, Roman law did not draw this terminological distinction.

2 Sohm, op.cit., 280. See also Jolowicz, Historical Introduction to the Study of Roman Law, 425.

Apart from formal contracts Roman law also recognised consensual contracts, iudicia bonae fidei. There it was not necessary to raise the exceptio doli expressly: exceptio doli iudiciis bonae fidei inest.[1] The iudex therefore automatically took into consideration dolus. He had to examine the legal relationship and determine the content of a party's obligations by reference to the objective norm of bona fides, or by what was bonum et aequum in the circumstances.[2]

According to Van Oven[3] defective consent was not in classical Roman law an independent ground for refusing enforcement of a consensual contract. By virtue of the implied exceptio doli the mere bringing of an action for enforcement of an improperly obtained contract constituted dolus, and was thus refused on the ground of being a violation of bona fides.

Roman law required bona fides in every stage of a contract: the causa or the foundation of the legal tie, the formation, and the performance. The existence and scope of a party's obligations were assessed by reference to what good faith required. As Powell said, bona fides defined "the whole complex of rights and duties between the parties in the particular transaction".[4] The good faith required of the parties often reflected commercial usage, but bona fides was a sufficiently flexible standard for it to be used to impose various duties on the parties in order to remain in tune with changing conceptions in society's values and customs.[5]

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1 D. 10.1.14; 24.3.21 and 30.5.84.

2 Kaser, op.cit., 142.

3 Wilsgebreken, goede trouw en oorzaak, W.P.N.R. 3240-3243.

4 Op.cit., 20.

5 De Zulueta, The Roman Law of Sale, 9.

Bona fides in Scots Law

(i) The institutional writers

The seventeenth and eighteenth centuries, when Roman law influence in Scotland was at its peak, were also the formative centuries of modern Scots law.[1] The imprint of Roman law on the developing Scottish legal system was thus necessarily extensive and this is nowhere more evident than in the law of contract.[2]

Scots law apparently accepted the Roman distinction between contracts stricti iuris and contracts bonae fidei. Craig's Jus Feudale showed strong Roman law influence and his exposition of bona fides was both one of the most unequivocal in the institutional writings and conceptually the most closely aligned to bona fides as it existed in Roman law.

> Contracts 'bonae fidei' are those which are interpreted in accordance with the fair and just intention of the parties even though they have not themselves fully expressed it. In construing them regard is paid rather to the intention of the mind than to the words employed. As Hotman puts it, it is as if the parties had agreed that their rights under the contract should be those which are fair and just in its circumstances. The class of contracts 'bonae fidei' includes all the mutual contracts, such as purchase and sale, lease, hire and those others which are enumerated by Justinian... /I/n this whole class of contract the reliance placed by the parties on the sincerity of each other's contractual intentions makes it necessary to ascertain the precise effect of their agreement by reference to that which is fair and just, and to that which is ordinarily done in similar transactions. In contracts 'stricti iuris'

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1 P. Stein, The Influence of Roman Law on the Law of Scotland (1957) 23 Studia et Documenta Historiae et Iuris 149, 158.

2 Ibid., 167-168.

> it would be a great mistake to suppose that considerations of good faith or of fairness and justice are put out of view; but considerations of that nature are restricted within narrower bounds and are controlled by the formal stipulations made by the parties. It is not therefore admissable to depart from the express terms of such a contract nor to add to them. All formal engagements are 'stricti iuris', such as cautionry and bail... /T/he contracts of lease, sale, and the rest, remain by our law contracts 'bonae fidei' as they were by the Law of Rome, each party being bound to fulfill all conditions required by good faith and justice according to the nature of the contract even though these conditions be not expressly mentioned.[1]

It is clear from the juxtaposition of contracts stricti iuris and contracts bonae fidei that in Scots law, as in Roman law, bona fides defined the rights and obligations of each party to the contract bonae fidei. Although the primary sources of the contractual content were to be found in the intention of the parties and common usage, the courts also had the power to depart from or add to the express terms of the agreement in order to attain a contract which corresponded more closely to the standard of what was "fair and just" in the circumstances.

Stair, although he maintained that "bonum et aequum" were the foundations of the whole caselaw of Scotland, made hardly any reference to bona fides. However, in his Institutions he wrote:

> The civil law gives so little to mutuum, by the nature of the contract, that it is amongst the contracts stricti iuris, where nothing is understood but what is expressed, or necessarily consequent therefrom: and therefore there is no annual or profit due in mutuo.[2]

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[1] I, 9, 33.

[2] I, 11, 6.

Stair evidently regarded mutuum in Scots law as also being stricti iuris, because he continued: "So we allow no profit in mutuo, unless it be so agreed upon".[1] The same strictness of interpretation applied to tacks, which Stair described as strictissimi iuris.[2] And in discussing mandate, he said that the "mandatar" who, unaware that the mandant had died, performed the mandate, had the exception bonae fidei.[3] The diligence required of a mandator was not the "exactest diligence" as Roman law would have it, but, in view of the fact that the undertaking is gratuitous, merely such diligence as the mandator would use in his own affairs, "but still there must be bona fides".[4]

In view of Craig's strong assertions as to the importance of bona fides in contracts, Stair's relative silence is all the more peculiar. His singling out, and implied acceptance of mutuum and tacks as stricti iuris probably indicates that they were worth special mention because they were exceptions to the general rule of contracts being bonae fidei. In view of Stair's numerous statements to the effect that bonum et aequum underlie Scots law[5] it is certainly far more plausible to accept this explanation than to take it that he denied the existence of a general standard of good faith in the Scots law of contract of the time.

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1 Ibid.

2 II, 9, 26.

3 I, 12, 6.

4 I, 12, 10. See also I, 9, 10 where Stair described the contract of sale as bonae fidei.

5 See, for example, I, 1, 18.

Bankton referred to the Roman law distinction between contracts bonae fidei and stricti iuris and concluded that "we have little use for this distinction",[1] not because bona fides was not known, but because "only Loan and Promises are strictly interpreted".[2] Contracts bonae fidei he described as those in which the judge has

> liberty to determine, upon the mutual obligations of the parties, from the nature of the contract, according to their presumed will, as in Sale, Mandate, Location and other enumerated by the Emperor /Justinian/[3]

Kames, discussing equity in Scots law, also referred to bona fides in contracts:

> Among persons who are swayed by interest more than by conscience, the employing indirect means to evade the effect of their engagements, is far from being rare. Such conduct, as being inconsistent with that candor and bona fides which is requisite in contracting, and in performing contracts, is morally wrong, and a court of equity will be watchful to disappoint every attempt of that nature.[4]

Kames also distinguished contracts bonae fidei from contracts stricti iuris and said that in the former "equity may interpose to correct inequalities, and to adjust all matters according to the honest intentions of the parties.[5] In the latter group nothing could be considered which was not part of the agreement. Contracts bonae fidei were those where the performance was merely a means to a further end, for example, where horses are purchased for the purposes of breeding. The horses had to be fit for breeding otherwise equity would intervene. Stricti iuris contracts were those in which the performance

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1 I, 11, 65.

2 Ibid.

3 Ibid.

4 Equity, 163.

5 Ibid, 120.

was an end in itself.[1]

Bell, the last of the institutional writers, was already strongly influenced by classical contract theory and it is therefore not surprising that bona fides, as a residual requirement for a valid contract, played no role in his writings at all.[2] However, in his Dictionary and Digest of the Law of Scotland he did refer to the Roman distinction between contracts bonae fidei and contracts stricti iuris, but he made no comment on its relevance to the Scots law of his time.

(ii) Seventeenth and eighteenth century caselaw

Seventeenth and eighteenth century case reports were brief and although they generally referred to the arguments of counsel, they gave no, or very few, reasons for the courts' decision. Yet, in a number of cases the contract in question was referred to as being either bonae fidei[3] or stricti iuris.[4]

In Fleming and Gibson v. Fleming and Baird,[5] B had accepted 12,000 merks as a tocher, by a contract of marriage, in satisfaction

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1 Ibid.

2 See, however, Principles, 474 where Bell described insurance as a contract of good faith.

3 Morison and Glen v. Forrester 1712 Mor. 14236 - emption vendition; Coutts & Co. v. Allen & Co. 9 January 1758 F.C. 144 - purchase and sale; Sword v. Robert and Alexander Sinclair, and Campbell 1771 Mor. 14241 - purchase and sale; Stewart v. Morison 1779 Mor. 7080 - insurance contract; Thompson v. Buchanan 1781 Hailes 886 - insurance contract; Kinloch v. Campbell 14 June 1815 F.C. 421 - insurance contract.

4 Duke of Lauderdale v. Lord and Lady Yester and the Earl of Tweeddale 1675 Mor. 6545 - reversions.

5 1663 Mor. 9148.

of all that his wife could succeed to by her family. However, as the wife's mother had earlier put more bonds in the wife's name she pursued B and his wife to grant an assignment of this sum and to repay the sums which he had used over and above that constituted by the tocher. The pursuer alleged that as this was a bonae fide contractus

> the meaning and interest of parties is most to be respected; and therefore, though it contains but expressly a discharge, which cannot be effectual to lift the sums from the creditors, but would lose them to both parties, he must assign; especially, seeing his acceptance of full satisfaction imports an obligement to denude himself of the superplus; and which the Lords found relevant, and sustained the summons.[1]

(iii) Bona fides after the rise of freedom of contract

The requirement of bona fides did not, as one would have expected, disappear entirely during the nineteenth century. Surprisingly little was heard of it in respect of the contract of purchase and sale[2] but it did make an appearance through the recognition that a warrandice existed in respect of the goods sold.[3] Lord Justice-Clerk Hope, charging the jury in Whealler v. Methuen expressed the principle as follows:

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1 Ibid. See also Wemysses v. Wemyss 1768 Hailes 238, where a marriage contract, although not signed, was held to be binding. "In marriage-contracts" Lord Auchinleck said, "the greatest honesty and fairness are required... Can this woman lie by for thirty or forty years, and then object to the formality of the contract, whereof she does not pretend that she was ignorant?"

2 See, however, Whitson's Trustees v. Neilson (1828) 6 S. 579 where the central question was whether the contract had been implemented in a manner consistent with bona fides.

3 See J.J. Gow, Warrandice in Sale of Goods (1963) 8 Jur. Rev. 31, and Mercantile and Industrial Law of Scotland, 161; Brown on Sale, 288.

> /T/he principle of the law of Scotland is, that every man selling an article is bound, though nothing is said of the quality, to supply a good article without defect, unless there are circumstances to show that an inferior article was agreed on. That is the implied warranty in law, and therefore the price agreed on is important, as showing the understanding of the parties. For when anyone sends an order for goods, without a word as to their quality, he is entitled to such an article, as the price entitles him to expect, of good, sound, fair quality.[1]

Although later in the nineteenth century insurance contracts, under the influence of English law, came to be referred to as uberrimae fidei, the courts early in that century apparently still regarded them as no different from most of the other types of contracts and they were referred to as being bonae fidei.[2] According to Bell[3] insurance was a contract of good faith because the insurer, in calculating the risks to be run, greatly relied on the statement of the insured.

Both Rankine[4] and Hunter[5] made spirited pleas that leases or tacks should be regarded as bonae fidei contracts and not stricti iuris as the institutional writers[6] had asserted. Both writers relied on a number of cases as authority for their views.[7] However, in many of

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1 (1843) 5 D.402, 406. See also the statement by the same judge in Paterson v. Dickson (1850) 12D. 502, 503.

2 Thompson v. Buchanan 1781 Hailes 886; Forbes & Co. v. Edinburgh Life Assurance Co. 9 March 1832 F.C. 351; Stewart v. Morison 1779 Mor. 7080.

3 Principles, 474.

4 Law of Leases in Scotland, 98.

5 Landlord and Tenant, Vol II, 149-152.

6 See, for example, Erskine II, 6, 31; Bankton II, 9, 11.

7 See, for example, Smith v. Robertson (1831)9 S. 751, 752; Ross v. Sutherland (1838)16 S. 1179, 1180; Wight v. Earl of Hopetoun (1858) 20D. 955, 958; Fraser v. Ewart 25 February 1813 F.C. 223.

these cases bona fides was given a limited role: It was no longer regarded as the norm by reference to which the parties' rights and obligations were determined. Bona fides at most functioned to prevent an unreasonable interpretation being given to ambiguous terms.[1] As Lord Curriehill said in Wight v. Earl of Hopetoun:

> /T/he court is not to alter the express stipulations of parties in any contract, yet it is a principle in our law that certain contracts are to be regarded as contracts in bona fide, and are to be construed so as to give effect to the probable intention of the parties.[2]

There is no doubt, however, that even in the second half of the nineteenth century bona fides could still be used to limit a party in the exercise of his right.

In Wemyss v. Wilson[3], the First Division affirmed the decision of Sheriff Monteith to award damages to a tenant of a farm on the ground that the landlord had increased the game on the farm beyond what was fair. Although there was no provision in the contract as to an increase in the game Sheriff Monteith based his judgment on the fact that a lease was a contract bonae fidei,

> and that as such it falls to be construed according to the understanding of the contracting parties at its date: Finds that the law does not recognise any right on the part of landlords to exercise their exclusive privileges in regard to the game upon their lands, in a manner inconsistent with the bona fides of contracts of lease existing between them and their tenants.[4]

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1 See, however, Stirling v. Miller 29 June 1813 F.C. 416 in which the court considered the effect of a clause in a tack to which a party had succeeded, stipulating personal residence. Lord Meadow-Bank declared that "/t/he clause must be construed reasonably, and with allowance for all contingencies. Now, here the party was detained by the hand of God, and unable to comply with the provision of residence, without any fault of her own. /It/ is to receive a fair interpretation, according to the course of human affairs" /419/

2 (1858) 20D. 955, 958.

3 (1847) 10D. 194.

4 Ibid., 195.

And in Morton v. Graham[1] a lease contained a clause reserving to the landlord "all game /etc./ with the exclusive liberty to him...of hunting, shooting, sporting and fishing on the premises, without being liable to compensate the tenant in respect of the reservation and liberty herein expressed." In an action by the tenant for damages caused by an increase in the game, the court held that as the parties had contemplated such an increase and it had not been extravagant, the pursuer could not succeed. However, referring to the rule set out in Wemyss v. Wilson[2] Lord President Inglis said:

> I think the great principle involved in that rule is, that something has been done by the landlord not contemplated in the contract of lease, and against the faith of the contract.[3]

As the parties here envisaged an increase, that rule was not applicable. The question here was whether the increase had

> been done to so unreasonable an extent as nevertheless to admit a claim of damages on the part of the tenant... /I/t was plainly contemplated that the agricultural tenant should suffer damage, but for that he was to have no claim. Still I can imagine a case of such extravagant and unscrupulous use of means to increase the game as would amount to a fraud on the agricultural tenant, and open to him such remedy as he here seeks... I think that where a tenant is by his lease declared to have no claim for compensation, unless he makes out a case amounting to bad faith on the part of the landlord he has no claim for damages.[4]

Lord Ardmillan reiterated these views by saying that the tenant was "bound by that clause according to its fair meaning, and with reference

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1 (1867) 6M. 71.

2 (1847) 10D. 194.

3 (1867) 6M. 71, 73.

4 Ibid., 73, 74.

to the state of the farm".[1]

Wemyss v. Wilson and Morton v. Graham were decided at a time when bona fides was generally being given a more restricted function and in an era which, on the whole,was hostile to general standards such as good faith. Yet they clearly illustrate the way in which bona fides was used to impose certain limitations on the rights arising from a contract. Looked at differently, it can also be said that, by virtue of the standard of good faith, the court imposed on the landlord an additional duty, to exercise his right reasonably.

In the Wemyss and Morton cases good faith fulfilled a role similar to that of implied terms in presentday law. In addition, those cases illustrate the way in which bona fides could have been employed to undercut unfair exemption clauses. However, that potential has not been realized. Although Gloag stated that "/it/ is a general rule that contracts are to be construed on the assumption of honest dealing"[2] the context in which this statement appeared clearly indicated that by "honest dealing" he merely meant subjective honesty and not that the rights and obligations of the parties would be determined or adjusted by reference to what an objective standard of bona fides required in the circumstances.

(iv) Conclusions

As far as it is possible to make any firm deductions from the evidence available on the subject, it would seem as if seventeenth and

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1 Ibid., 75.

2 Op.cit., 400.

eighteenth century Scots law accepted the distinction between contracts bonae fidei and contracts stricti iuris. Most contracts were regarded as bonae fidei: mutuum, tacks and possibly "transaction"[1] (compensation) being the exceptions. In the case of stricti iuris contracts, the creditors could insist on performance according to the precise terms of the agreements. In bonae fidei contracts, however, the court, in assessing the scope and content of the rights and obligations of the respective parties, had to do so by reference to what bona fides required. This process involved more than a mere interpretation in good faith of the terms of the agreement. It meant that the court, in deciding the manner in which the agreement was to be implemented - or applied in the concrete situation - could, by virtue of the residual requirement of bona fides, add to or depart from the terms agreed on by the parties. As Craig said, "it is as if the parties had agreed that their rights under the contract should be those which are fair and just in the circumstances".[2] In essence this meant that a creditor could only rely on a contractual right and claim performance in terms of the agreement if it was consistent with bona fides to do so. That did not entail that the agreement reached by the parties was worthless or that what bona fides required in a particular situation was determined solely by the courts subjective view of fairness. In Scots law, just as in Roman law, bona fides was an objective standard and the intention of the parties, commercial usage and the mores of the community were the most important referents of that standard.

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1 Smith, op.cit., 297.

2 I, 9, 33.

Bona fides was still referred to in a few early nineteenth century cases, as well as in some treatises. Wemyss v. Wilson[1] and Morton v. Graham[2] showed that even in the second half of that century a court could still to some extent define parties' rights and obligations by reference to good faith requirements. However, in most of the nineteenth century caselaw bona fides was used in a narrow sense, to mean that contract terms, if ambiguous, should be construed so as to have a reasonable rather than an unreasonable effect.

Even during the seventeenth and eighteenth centuries the requirement of bona fides never appears to have been very clearly circumscribed or consistently applied so that it is not surprising that it fell into disuse during the reign of freedom of contract. As there is virtually no reference to an overriding standard of bona fides to be found in the late nineteenth and twentieth centuries it can only be surmised that the entire concept had contracted to become merely a canon of construction. As it had become completely subordinated to the principle of freedom of contract it lost its effectiveness as an instrument through which contractual fairness could be promoted. However, bona fides, as a residual requirement for a valid contract has not been abolished by statute or authoritative decision[3] and could possibly be resurrected by an enterprising court.[4]

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1 (1847) 10D. 194.

2 (1867) 6M. 71.

3 Scottish Law Commission, op.cit., 142-143.

4 In South African law, for example, the exceptio doli has recently been resurrected as a ground for refusing enforcement of contractual rights which would otherwise have caused great injustice: See Novick v. Comair Holdings Ltd., 1979(2) S.A. 116 (WLD); Rand Bank Ltd. v. Rubenstein 1979(2) S.A. 848 (WLD).

It was pointed out that in Roman law bona fides, whether intrinsically as in the case of iudicia bonae fidei or through the exceptio doli as in the case of stricti iuris contracts, was required in every stage of a contract, from its formation to its performance. It is, on the other hand, a common feature of both Scots institutional writing and judicial utterances on the subject of bona fides that reference was made predominantly to the relevance of good faith in respect of the process of determining the content of the parties' rights and obligations and to the implementation of the agreement. The fact that bona fides was hardly mentioned in relation to the formation of contracts in Scots law does not mean that it was not required in that field. It merely means that with the rise of the individual will or intention as the basis of contractual liability, the function fulfilled in that area by bona fides in Roman law was, in seventeenth century Scots law, taken over by the notion of consent.[1] The rise of the will theory, caused the link between fraud, vis ac metus and error, and the good faith principle to be severed and the latter's sphere of influence to be confined to the implementation of the contract. The substitution of the specific defects, fraud, error and vis ac metus, for the general, violation of bona fides, was a formal process, attributable to the newly found importance of consensus rather than to any fundamental change of policy. There was and is no necessary conflict between the requirement of consensual propriety and that of good faith. As Abas rightly pointed out, the cases where a party will truly consent to enter into what is for him a highly disadvantageous transaction, are extremely rare.[2]

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1 Cf. Abas, Beperkende Werking van de Goede Trouw, 76.

2 Ibid., 76-77.

At first sight it would not seem as if fraud, error and force and fear would be wide enough to cover all the improprieties which Roman law could categorise simply as violations of bona fides. Yet, when the nature of fraud, as set out by the institutional writers, is examined it becomes clear that, like Roman dolus, it had the character of a residual category, growing in meaning and content as new manifestations of improper conduct were classified as fraud.

The most widely accepted definition of fraud was that given by Erskine: "a machination or contrivance to deceive".[1] This already broad notion of fraud was further expanded by the custom of inferring fraud from the facts of a particular case. Stein said that

> /S/uch cases were justified as being lata culpa quae dolo aequiparatur: 'for the difference betwixt dolus and lata culpa is that dolus est magis animi, and oftentimes by positive acts, and lata culpa is rather facti, and by omission of that which the party is obliged to show.[2]

By this device the category fraud[3] was broadened to include not only conscious misrepresentation and concealment but things as diverse as the conclusion of contracts by insolvents, the exploitation of the facile, the weak, the necessitous and the inexperienced, as well as the so-called pacta contra fidem tabularum. It can thus be said that in seventeenth and eighteenth century Scots law, fraud functioned as a residual category akin to dolus in that it provided the courts with a

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1 III, 1, 16.

2 Stein, Fault in the formation of contract in Roman law and Scots law, 173 citing Stair I, 9, 11.

3 See generally McBryde, Void, Voidable, Illegal and Unenforceable Contracts in Scots Law, 71-92.

ground on which to denounce any agreement which the courts regarded as unjust. Since that era the concept of fraud has been whittled down. In addition many of the instances covered by fraud have evolved into independent grounds of reduction. Some of those will be examined in the following sections.

3 - EXTORTION

Although Scots law has, with a few exceptions[1], proved unwilling to relieve from contracts merely on the ground of inequality in the exchange, there are statements by the institutional writers and in reported cases which suggest that a contract may be so extortionate in its terms that reduction of it is justified even though there was no fiduciary relationship between the parties, nor improper practice, nor a legal defect in capacity.[2] However, neither the institutional writers nor the courts have dealt with the problem of such extortionate contracts in a uniform manner. Two approaches have been adopted: on the one hand, relief has been given on the basis that an unfair contract could be attributed to, or explained by, a bargaining weakness of the disadvantaged party. In such a case it was apparently assumed that the benefiting party had exploited the particular bargaining handicap of the other by taking from the latter an unfair advantage. On the other hand, the courts have reduced contracts on the ground of fraud which was inferred principally from the inequality of the parties and the lesion suffered by the inferior party, or from enorm lesion in itself.

For his opinion that extortionate contracts may be reduced Gloag relied primarily on Stair, who despite his assertion that an article has no value other than that agreed on by the parties,[3]

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1 Ante, 174-178.

2 Gloag on Contract, 492-493. See also Walker, Principles of Scottish Private Law, Vol. I, 597; Walker, Equity in Scots Law, 346-347; Smith, Short Commentary on the Law of Scotland, 839.

3 I, 10, 14.

maintained that there may be circumstances in which the court may compel a person to sell his goods at a "just price". This can occur for example,

> if the buyer take advantage of the ignorance and simplicity of the seller, and where there is no alteration of the common rate, nor ground thereof asketh or taketh more ... /or/ when ware is kept up till pinching necessity. ... or when some special necessity of an acquirer puts him so upon the mercy of the disponer, that he may take a price, even above that which himself accounts the thing worth.[1]

To Stair the mere fact that there was no deceit on the part of the disponer is of no consequence. What is required for judicial intervention is that the seller exploited or took advantage of the difficulties of the buyer, to the latter's financial detriment. The court may intervene even though the buyer knowingly paid more for something than it was worth. The court, having found the contract to be "extortionate" may then either reduce it completely or adjust the price so that it conforms to what is just in the circumstances.[2] The just price will normally be the "common"[3] price, that is the market price.

A few cases exist in which the courts acted on principles similar to those set out by Stair. In Murray v. Murray's Trustees,[4] the pursuer, a young and inexperienced man, received £400 through a legacy from his uncle, to whom he was also heir at law. He was subsequently approached by the trustees of his uncle's property, who

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[1] I, 10, 15.

[2] Ibid.

[3] I, 10, 14.

[4] (1826) 4S. 374.

requested him to renounce his legal rights as heir. He complied as he was under the impression that his uncle wished to disinherit him completely. As there was some doubt about the validity of this deed the pursuer was asked to subscribe to another deed of renunciation. He again complied, ostensibly "from feelings of gratitude and regard for his deceased uncle, and from a conviction of the probably ruinous effects to all parties of any attempt to disturb the settlements of the defunct."[1] The Lord Ordinary, discussing the reduction of these deeds, referred[2] with apparent approbation to the cases of Lochiel's Trustees[3] and M'Neill v. M'Neill[4], and said that

> /T/hese cases seem to lead to the conclusion, that, without being obliged to establish facility, a very unequal transaction entered into, by which a great advantage has been obtained by one of the parties from the ignorance or want of experience of the other, who ought to have been invited to seek the aid of a friend or a man of business to advise with, may be set aside.[5]

On appeal, the court affirmed the decision of the Lord Ordinary and refused to sustain the deeds on the ground that they had been procured from an ignorant and inexperienced young man without the benefit of deliberation or advice and that he had been taken advantage of.[6]

And in Ewen v. Magistrates of Montrose[7] where a father had obtained a discharge of his obligations from his married daughter for a grossly inadequate consideration, the House of Lords reduced the

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1 Ibid., 375.

2 Ibid., 377.

3 8th July 1795.

4 January 1816.

5 (1826) 4S. 374, 377.

6 Ibid., 378-380.

7 (1830) 4W. & S., Sc.App. 346.

contract on the ground that the father had taken advantage of his daughter's anxiety about her and her husband's imminent departure for India and of the financial distress of his son-in-law.[1]

A similar approach was followed in M'Donagh v. MacLellan[2], where in an action by an employee for compensation for injuries suffered in the course of his duties, the employer relied on a document signed by the employee, stating that he had received £8 in full compensation. The Lord Justice-Clerk Moncreiff held that although the employee had signed the document and had thus formally assented to the transaction, that fact did not exclude an additional claim, as there was ample evidence that the employee was an unsophisticated and illiterate man and "the parties /were/ not altogether upon an equal footing".[3] The employee was inferior to the other in rank and did not have the same facilities for considering the document. Where that is the case the party suffering from the insufficiency of understanding must be made perfectly aware of the effect of his actions.[4] And in Gilmour, Morton and Co. v. Bolland,[5] the Lord Ordinary (Lord Johnston) similarly held that a discharge of all future claims, given by a man who could neither read nor write and which was signed for him by an agent of his employers, was ineffectual.[6]

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1 Ibid., 357 per Lord Wynford.

2 (1886) 13 R.1000.

3 Ibid., 1002.

4 Ibid.

5 1906, 14 S.L.T. 583.

6 See, however, Welsh v. Cousin (1899) 2F. 277, where Lord Kyllachy maintained that the question was not whether the grantor read or understood a document, but whether he was capable of doing so and being so, signed it voluntarily.

These cases illustrate that lesion which can be traced to and explained by the necessity, dependence, inexperience, insufficient knowledge or understanding of the disadvantaged party, may provide a basis on which the contract can be set aside. Some cases leave one with the impression that an unfair contract may be insulated from attack if the stronger party has made perfectly sure that the inferior one is fully informed as to the nature and effect of the agreement. Informed consent may thus save an unfair bargain from being struck down. This raises the important question of the standard of explanation or enlightenment that a party is bound to provide - is it such as would remove the misunderstanding from a reasonable man or is the test subjective? Although the courts did not directly address themselves to this question, it would seem as if the character of the party in question can not be left out of consideration. In addition, judicial dicta suggest that an unfair contract may be enforced if the inferior party was given the benefit of independent advice.

In contrast to the case where a party is taken advantage of because of his insufficient understanding is the situation highlighted by Stair, namely where a party is compelled by his necessity to conclude the agreement. In such a case there can be no question of insulating the contract from attack by providing the disadvantaged party with independent advice or by explaining to him the effect of the terms. Indeed, Stair acknowledged that a person may knowingly have to submit to onerous terms in such circumstances.

So, in Anstruther v. Wilkie[1] the court reduced an undertaking

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[1] (1856) 18D. 405. This case is also sometimes cited as authority for the recognition of undue influence in Scots law.

by a "needy embarrassed, destitute client" to give £1,000, ostensibly as a gift, to his agent. Lord Justice-Clerk Hope declared that this was obviously no gift, but a sum extorted as an extra reward for services.[1]

> Advantage of the embarrassed condition of the client's affairs the agent shall not take for his own interest, and in order to obtain gifts, as this is called, for himself, on the condition of ordinary professional aid, as here, in obtaining a loan, which the pressing embarrassments of the client required to be immediately procured, to relieve him from destitution or personal diligence.[2]

Later writers, while pursuing a similar aim, proposed a different approach to that set out above. Bankton, Erskine, and later also Bell, postulated fraud as the basis of judicial intervention. Such an approach was, of course, facilitated by the wide meaning given to fraud in Scots law.[3] Fraud was not only defined widely, but was further expanded by the custom of inferring fraud from the facts of a particular case. Although Stair expressed the opinion that "/f/raud is not to be presumed, but must be proven",[4] Stein[5] pointed out that this view was by implication contradicted by Stair himself. Bankton was less ambiguous than Stair: he maintained that

> /f/raud is either in the thing itself, and signified the enormous Lesion or Prejudice sustained by one, even tho' there was no fraudulent purpose in the other to wrong him.[6]

He added:

> Deceit is never presumed, but must be clearly proved ... But sometimes the deeds themselves, without any proof of actual Circumvention, shall infer fraud, and a design to deceive;

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1 Ibid., 415.

2 Ibid., 416.

3 See generally ante, 196-197.

4 I, 9, 11.

5 Fault in the Formation of Contract in Roman Law and Scots Law, 173.

6 I, 10, 63.

> as when there is Great Lesion in the case, the deed bearing an affected recital, or otherwise being liable to suspicion, and the granter a weak person.[1]

And according to Erskine

> All bargains which, from their very appearance discover oppression, or an intention in any of the contractors to catch some undue advantage from his neighbour's necessities, lie open to reduction on the head of dole or extortion, without the necessity of proving any special circumstance of fraud or circumvention on the part of that contractor.[2]

Fraud, therefore, comprised not only the well-known incidents of fraudulent misrepresentation and concealment, but also a variety of transactions in which the courts were of the opinion that it would be inequitable for a party to benefit from the contractual rights which he had obtained. It is clear that the concept of fraud as espoused by the institutional writers and in some judicial dicta, was not confined to questions relating to the propriety of the formation of the contract, but was concerned also with the objective merits of the agreement.

Even before the time of Bankton there were cases in which the courts expressed the opinion that enorm lesion coupled with a bargaining weakness could indicate dolus in re. In 1696 in Alison v. Bothwell[3] the court held that a bargain stipulating for a grossly unequal exchange and made with a simple young man constituted dolus in re and could therefore be adjusted in order to repair the damage. And in Gordon v. Crauford and Crauford[4], a disposition of an estate worth £220 per annum for a price of £120, made by a person who was

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1 I, 10, 66.

2 IV, 1, 27.

3 1696 Mor. 4954.

4 1730 Cr.S. & P. 47.

necessitous and in debt, was set aside. The pursuer had argued that the transaction should be set aside on the basis of fraud and circumvention and the court accepted this argument, inferring fraud from the distressed state of the grantor, the deceitful terms of some of the writing and the great inequality of the bargain.

The practice of inferring fraud from the extortionate terms of the contract continued into the nineteenth century. In the previously cited case of Murray v. Murray's Trustees,[1] Lord Hermand declared that

> /T/he very nature of the deed itself shows that he must either have been an idiot, or must have been imposed upon; and as I am of opinion that it was obtained under the influence of ignorance and deception, it is impossible that I can sustain it.[2]

And in Tennent v. Tennent's Trustees[3] Lord Westbury expressed the relevant principle as follows:

> /T/here is an equity which may be founded upon gross inadequacy of consideration. But it can only be where the inadequacy is such as to involve the conclusion that the party either did not understand what he was about, or was the victim of some imposition.[4]

At the same time, however, there is evidence of a hardening of attitude in the nineteenth century. In M'Kirdy v. Anstruther,[5] for example, a person in great financial need sold a contingent interest in a succession for one quarter of its value. Lord Gillies

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1 (1826) 45, 374.

2 Ibid., 378-379.

3 (1870) 8M.(H.L.) 10.

4 Ibid., 26.

5 (1839) ID. 855. See also A.B. v. Joel (1849) 12D. 188; Mathieson v. Hawthorns & Co. Ltd. (1899) 1 F. 468; Caledonian Railway Co. v. North British Railway Co. (1881) 8R.(H.L.) 23.

declared that inadequacy of consideration was not per se sufficient to reduce a transaction, but that the price may be so grossly inadequate that it is evidence of facility on the part of the seller and circumvention on the part of the buyer. But his Lordship made it clear that in such a case the transaction would be reduced because facility, circumvention and lesion were all present. The court declined to intervene because both the seller and the buyer were men of full discretion and intelligence, dealing fairly and openly towards each other.[1]

The practice of inferring fraud from enorm lesion fell into disfavour in the nineteenth century primarily because, under the influence of freedom of contract, the concept of fraud was interpreted far more restrictively than it had been in the previous century and a half. Although, therefore, mere inadequacy of consideration was unlikely to lead to a presumption of fraud "/such inadequacy /would still/, no doubt, form a very important element in considering the question whether there has been fraud."[2] In M'Lachlan v. Watson[3] the Lord Ordinary (Lord Mackenzie) admitted that the bargain under scrutiny was a very hard one, yet he refused reduction on the ground of extortion, because the agreement had been entered into with full knowledge of its terms, and freely and voluntarily; the contracting

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1 Ibid., 863.

2 M'Lachlan v. Watson (1874) 11 S.L.R. 549, 550.

3 Ibid.

party was "of undoubted capacity, and in a position to act and judge for himself; and that he did so, perfectly understanding what he was about."[1]

It would therefore seem as if the power of the courts to set aside unfair transactions on the ground of fraud or exploitation of a party's bargaining handicap was interpreted more and more restrictively in the course of the nineteenth century. Gloag[2] cited only two comparatively recent cases in support of his view that inequality of the bargain could in itself lead to an inference of fraud, Young v. Gordon[3] and Gordon (Gordon's Administrator) v. Stephen.[4] However, although the courts reduced the contracts in both these cases, the bases on which they proceeded were not clearly stated.[5] Since then this jurisdiction has apparently passed into desuetude.

Despite some references to the contrary by Erskine[6] it has been authoritatively stated[7] that the Chancery jurisdiction against catching bargains with expectant heirs was not transplanted into Scots law.

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1 Ibid. 551

2 Op. cit., 492-493.

3 (1896) 23 R. 419.

4 1902, 9 S.L.T. 397.

5 Both these cases are discussed in greater detail, ante, 175-176.

6 IV, 1, 27.

7 M'Kirdy v. Anstruther (1839) 1 D. 855, 863.

4 - FACILITY AND CIRCUMVENTION

Stair made no mention of a separate and distinct doctrine of facility and circumvention and neither did Bankton or Erskine. Nevertheless, the latter two hinted in somewhat uncertain terms at the power of the courts to reduce lesionous contracts concluded with facile parties.[1] Bell was the only one of the institutional writers who made a distinct reference to facility and circumvention in the form in which it was to become known in modern times:

> The deeds of persons of full age, not cognosced, nor interdicted, may yet be reduced on showing evidence of weakness of mind, combined with fraud (or circumvention, as it is called in this instance) and lesion... /F/acility alone, where the person has understanding enough to save himself from a sentence of idiotry, is not a sufficient ground of challenge; and still less is lesion by itself, or gross inequality. But where lesion and facility concur, or where facility and circumvention appear, or even where there is lesion so gross as to indicate the other two qualities, a deed of conveyance or contract will be reducible. Such cases must, of course, depend on their own circumstances, and scarcely can be brought under any general rule of law.[2]

The protective policy of the courts operates in respect of both agreements inter partes, and testamentary dispositions of property. The principles of what later came to be known as facility and circumvention derive from the wide notion of fraud which Scots law recognised in the seventeenth century. As early as 1669 in Trinch v. Watson[3] the court reduced a disposition on the ground of fraud and circumvention, which

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1 Bankton I, 10, 66; Erskine IV, 1, 27.

2 Commentaries I, 136.

3 1669 Mor. 4958.

was inferred entirely from the fact that the grantor was weak, stupid and half deaf, coupled with the great inequality of the bargain. A few years later in Galloway v. Duff[1] the court reduced a disposition, again on the ground of fraud and circumvention, while stating in support of this finding that the defender had ordered the dispositions to be drawn up and that these were not read to the pursuer. The disposition, which consisted of a tenement, some bonds and all the pursuer's moveables, was made after the pursuer had been bleeding at the nose for days and while she thought she was going to die.

The practice of inferring fraud and circumvention where a facile party had been induced into a highly disadvantageous agreement was followed in subsequent cases[2] and almost a century later fraud was still the customary ground for reducing such transactions. In Mackie v. Maxwell,[3] an heiress who was prone to drunkenness sold her lands to her sister. The sister thereupon came to court to ask for reduction of certain dispositions of land which some people, mostly innkeepers, had elicited from the seller as payment for her liquor purchases. In evidence it transpired that the seller would have sold all her property

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1 1672 Mor. 4959.

2 Maitland v. Fergusson 1729 Mor. 4956, affirmed in Fergusson v. Maitland (1732) 1 Paton 73 - a deed reduced on the head of fraud which was principally inferred from the facility of the grantor coupled with the great inequality of the bargain. Contra: Swintoun v. Hay 1679 Mor. 4962; Gordon v. Ross 1729 Mor. 4956, where reduction was refused because no fraud on the part of the defender was proved.

3 1752 Kames 25.

in order to get drinking money, and that the challenged dispositions were not given for an adequate cause. The court reduced the dispositions on the ground of fraud and circumvention. However, Kames, commenting on the decision, denied that there was any evidence of fraud and circumvention. The real basis of the judgment, he contended, was that

> /I/t is certainly unjust to take advantage of weak persons, who cannot resist certain temptations; and to make use of such temptations to rob them of their goods. Let us examine the foundation of a judicial interdiction. It is nothing but a notification to the lieges of the weakness of the person interdicted, and to caution them against dealing with that person, unless upon an equal footing. It was therefore wrong in the defenders to take advantage of the known facility of Jean Mackie, and to elicit from her dispositions for a song, at least far under the true value. Where a weak person makes a deed, perhaps foolish, but voluntary,[1] in favour of any person who is entirely passive, such a deed admits of a very different construction. It is not reducible, however strong the lesion may be.[2]

By the late eighteenth century the practice of inferring fraud principally from the facility of one party coupled with the inequality of the transaction, began to meet with some criticism. In Robertson v. Fraser[3], a reference was made to two cases[4] in which the Lords held that facility and lesion, without specific averments of fraud, were sufficient to reduce a transaction. In the Robertson case itself no fraud other than that which could be inferred from the deed itself, was

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1 Kames was not correct if he implied that reduction would be refused in all cases where a deed was made voluntarily. In the Mackie case, for example, relief was given despite the fact that the seller herself admitted that the deeds were made voluntarily.

2 1752 Kames 25-26.

3 (1777) 5 B.S. 566.

4 The cases are referred to in the report as Dallas v. Dallas and MacDonald of Shian v. MacPherson of Killiehuntly.

alleged and the Lord Ordinary (Monboddo) thought that insufficient and refused to allow proof of the reasons for reduction. The Lords, on the other hand, allowed a proof and Lord Gardenston even went so far as to hold that facility and lesion were, per se, sufficient grounds for reduction.

The authority of the Robertson case was not strong enough to change a practice which had, over such a long period of time, become so deeply ingrained and the custom of inferring fraud continued in some cases,[1] even well into the nineteenth century. However, it was clear that the judicial attitude to the concept of fraud was changing and that the prevailing tendency was to restrict its sphere of application. Such an approach was no doubt more consistent with the classical theory of contract which was beginning to hold sway at that time.

However, as could be expected during a time of change, the general picture that emerged as regards the doctrine in the first half of the nineteenth century was a conflicting one. There were dicta in some cases which pointed to a stricter approach. In Scott v. Wilson,[2] for example, Lord Pitmilly declared that

> /t/he pursuer must make out facility to the extent law /sic/ holds necessary - he must also prove lesion - and likewise that all was done by fraud and circumvention. Facility to a great extent, and lesion to the greatest amount, are not sufficient without fraud and circumvention... At the same time, if the facility and lesion are great then slighter proof of fraud and circumvention are sufficient, which is the only limitation I can make of the doctrine.[3]

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1 See, for example, White v. Ballantyne (1823) 1 Shaw's App. 472; McIlwham v. Kerr (1823) 2S. 240; Gibson & Others v. Watson & Others (1827) 2 W. & S. 648; McDiarmid v. McDiarmid (1826) 4S. 583; affirmed in (1828) 3 Bli. N.S. 374. Contra: Scott v. Archibald and Others 1789 Mor. 4965; Morrison v. Morrison (1841) 4D. 337.

2 (1825) 3 Mur. 518.

3 Ibid., 526-527.

At the same time the tendency to infer fraud and circumvention primarily from the facility and the lesion continued. In McNeill v. Moir[1] there was proof of facility and enormous lesion, but not of fraud. Nevertheless, the court declared that

> the transaction upon the face of it appeared so grossly unequal and irrational, that it was plain that it could only have been brought about by a fraudulent advantage having been taken of his facility.[2]

However, the whittling down of the concept of fraud in the nineteenth century made it increasingly difficult to continue to give relief on the ground of fraud in circumstances where no positive acts of deceit were averred. At the same time the Court of Session proved unwilling to limit the jurisdiction to that extent. The result was that in Clunie v. Stirling[3], Lord Justice-Clerk Hope held that separate issues of facility and circumvention on the one hand and fraud on the other, should henceforth be granted.

After Clunie v. Stirling the established form of issue in these cases was:

> whether....the pursuer was weak and facile in mind, and easily imposed on; and whether the defenders.... taking advantage of the pursuer's said facility and weakness, did, by fraud or circumvention procure the deed or minute of agreement,... to the lesion of the pursuer.[4]

Although fraud continued to be included in the issue it was a much more restricted species than the concept on which relief had earlier been

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1 (1824) Shaw's App. 206.

2 Ibid., 211-212.

3 (1854) 17D. 15, 19.

4 McCulloch v. McCracken (1857) 20D. 206, 210.

based. In effect, therefore, the jurisdiction had, by the second half of the nineteenth century, gained an existence independent of the prevailing notion of fraud. In order to be given relief it was necessary to prove facility, fraud or circumvention, and lesion.

(i) Facility

The early cases,[1] where they did not refer merely to the weakness or facility of a party without more, alluded almost exclusively to physical impairment as evidence of facility. It was only in the nineteenth century that the courts began to regard facility primarily as an impairment of the mind.[2] Although the source of facility was still predominantly the physical debility of a party the term was then used to denote that state of mental weakness which arose from such debility. The meaning of the term was further explained by Lord Moncreiff when he said that the question of facility

> does not depend altogether on the state of the mind in respect of mere intellect or understanding. It rather regards the state of the mind morally and constitutionally, whereby it may be liable either to undue influence induced by fraudulent pretences or to intimidation under peculiar relations between the parties.[3]

The quintessence of facility is thus the fact that as a result of his mental state a party is susceptible to imposition or as Lord Justice-Clerk Hope in Clunie v. Stirling expressed it, is "ready to yield his assent".[4]

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1 See ante, 209 and accompanying footnotes.

2 See the cases referred to in footnote 1, page 211.

3 Cairns v. Marianski (1850) 12D. 1286, 1290.

4 (1854) 17D. 15, 17.

The requirement of facility has been very liberally interpreted at times. In Gibson and Others v. Watson and Others,[1] a deed of settlement executed by a woman who was found to be capable of disposing of her estate was reduced because she was not in such a state of mind as to appreciate that the effect of the deed was to deprive her of all her power of revoking or altering it. And in McKellar v. McKellar,[2] a testator who had a "lack of fixity of purpose" was found to be facile despite being able to conduct his other business quite satisfactorily. The Lord Justice-Clerk Inglis in Morrison v. Maclean's Trustees, in charging the jury, expressed the opinion that a man may be "facile for want of judgment or reason, another man may be weak and facile from mere nervousness and incapacity to resist solicitation".[3] These dicta show a considerable watering down of the requirement of facility, but it is doubtful whether they can be regarded as representative of a new direction. The view expressed by Lord Justice-Clerk Alness in his dissenting judgment in Gibson's Executors v. Anderson, that facility connoted pliability and meant that "a person is in such a mental state that he is unable to resist pressure, and that someone else can mould and fashion his conduct as he pleases"[4] was rejected with some vehemence by Lord Blackburn[5] in the same case. Lord Blackburn instead accepted the definition of facility given by Bell in his Dictionary and Digest of the Law of Scotland:

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1 (1827) 2 W. & S. 648.

2 (1861) 24D. 143.

3 (1862) 24D. 625, 635.

4 1925 S.C. 774, 790.

5 Ibid., 787.

> a condition of mental weakness, short of idiocy, in which an individual is easily imposed upon and induced to do deeds to his own prejudice[1]

On the whole, the courts have been reluctant to expand the scope of facility by discarding the requirement of a weakening of the mental faculties.[2] However, in Gray v. Binny,[3] Lord Deas was of the opinion that facility

> may arise from many different causes, temporary or permanent - for instance, from old age, exciteability, timidity, sickness, or, as in this case, from affection.

(ii) Lesion

A contract will only be reduced where the pursuer has relevantly averred that he suffered lesion as a result of it. Lesion is serious loss, damage or detriment incurred as a result of the transfer of property or rights whether gratuitously or in a contract for consideration. Where the lesion is great, the requirement of circumvention will be inferred more readily.[4] In addition, substantial lesion may also to some extent be regarded as evidence of facility.

(iii) Circumvention

From the late seventeenth century until well into the nineteenth century "fraud and circumvention" was generally inferred from a party's

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1 Ibid.

2 In Gray v. Binny (1879) 7R. 332, 346, Lord Shand expressed the opinion that where there was no averment of mental impairment "facility" was not the appropriate term.

3 (1879) 7R. 332, 350. See also Clunie v. Stirling (1854) 17D. 15, 17 per Lord Justice-Clerk Hope.

4 Munro v. Strain (1874) 1R. 1039, 1048; Mackay v. Campbell 1966 S.C. 237, 249.

facility and his lesion. In the intellectual climate of the nineteenth century the earstwhile wide concept of fraud was radically curtailed. It was then thought that fraud could only be found if there had been averments of positive acts of deceit. Naturally, such a notion of fraud conflicted with the species on which reduction had customarily been based and, if it had been required, would have severely restricted the scope of the jurisdiction. In order to protect its jurisdiction the Court of Session, therefore, held that reduction would be granted if facility, lesion and fraud and/or circumvention were to be relevantly averred.[1] This approach has persisted[2] despite some attempts by the House of Lords[3] in the latter part of nineteenth century to impose a requirement that fraud proper had to be proved.

However, in 1966 the House of Lords again intimated that where the grantor of a deed was alive, circumvention would not be found unless there was proof of deceit or dishonesty.[4] Such an opinion is contrary to the established principles of facility and circumvention and it is submitted that it should not be followed.

The juxtaposition of fraud and circumvention, of course, raised the question as to the precise meaning of circumvention. In Gibson's Executor v. Anderson, Lord Hunter defined circumvention as "the

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1 Clunie v. Stirling (1854) 17D. 15; McCulloch v. McCracken (1857) 20 D. 206.

2 Munro v. Strain (1874) 1R. 1039; Horsburgh v. Thomson's Trustees 1912 S.C. 267; Gibson's Executor v. Anderson 1925 S.C. 774. Mann v. Smith (1861) 23D. 435.

3 Marianski v. Cairns (1852) 1 Macq. 212. See also Lord Anderson in McDougal v. McDougal's Trustees 1931 S.C. 102, 116.

4 1967 S.C. (H.L.) 53.

impetration of a will or deed against a person's interest",[1] and Lord Kyllachy, in the unreported case of Parnie v. Maclean, said that

> fraud and circumvention are two shades of the same thing, the meaning of the issue being that you have the question put to you whether, facility existing, there had been either distinct machinations, tricks, importunities, solicitations, even suggestions, towards the testator while the testator's facility was such that she was not in a position to resist - not likely to be in a position to resist. It is not necessary that there should be deceit. It is enough that there should be solicitation, pressure, importunity, even in some cases, suggestion. The degree of circumvention would depend on the degree of facility.[2]

However, there is seldom any direct proof of any of the acts of circumvention enumerated by Lord Kyllachy and the courts have recognised this by maintaining that "/t/he existence of such acts of impetration must always be a matter of inference".[3] In Cleugh v. Fleming Lord Sorn justified this practice as follows:

> In circumstances which do not lend themselves to the suggestion of impetration, it might be that the Court would refuse to entertain an action in the absence of some specific averment of circumvention. On the other hand, where circumstances do lend themselves to the suggestion, the general averment may be treated as enough to entitle the aggrieved person to have the matter tried out. Were it otherwise, you might have a case in which the surrounding circumstances all pointed irresistibly to impetration and yet in which the aggrieved party would have no remedy because, not being privy to the fraud, he could not specify the actual form of suasion used.[4]

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1 1925 S.C. 774, 783.

2 Cited by Lord Blackburn in Gibson's Executor v. Anderson 1925 S.C. 774, 778.

3 Ibid., 783 per Lord Hunter.

4 1948 S.L.T. (Notes) 60.

In Clunie v. Stirling, Lord Justice-Clerk Hope listed some of the surrounding circumstances from which circumvention may be inferred:

> /T/he result may demonstrate that the party was really circumvented... when he was led into the transaction under challenge; and then the nature of that transaction, the mode in which, and the party by whom it was carried through, and the object apparent on the face of it, for which, if palpably disadvantageous, it was huddled up without proper inquiry, and without the individual receiving the aid he ought to have received, all bear on the jury question, whether the party had been circumvented.[1]

The paramount importance of the result and nature of the transaction in the process of inferring circumvention is illustrated by the actual decision in the Clunie case where both Lord Justice-Clerk Hope and Lord Blackburn found circumvention proven on the evidence only of the "ruinous" and lesionous bargain. There was no evidence whatsoever of any of the acts of impetration mentioned by Lord Kyllachy. The same was true of the decision in Gibson's Executor v. Anderson[2] and most of the other cases in this survey. When such evidence is available the proof of circumvention will, of course, be all the stronger, but the absence of evidence as to impetration will not necessarily preclude the courts from making a finding of circumvention.

There is also a close relationship between the requirements of facility and circumvention, which is reflected in the rule that the greater the facility the less is the proof of circumvention which will be required, and where proof of circumvention is strong the degree of facility required will be comparatively less.[3]

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1 (1854) 17D. 15, 17.

2 1925 S.C. 774.

3 Munro v. Strain (1874) 1R. 1039, 1047 per Lord Ormidale.

5 - UNDUE INFLUENCE

A partial reception of the English law concept of undue influence has taken place in Scots law.[1] In England the term undue influence has a double meaning;[2] when used in relation to wills an element of coercion is required. Coercion is, however, not a necessary element when undue influence pertains to transactions inter vivos. In contrast, undue influence exists in inter vivos transactions where, in a relation of confidence and trust between the parties, the one in whom the confidence is reposed, uses such personal influence to the detriment of the confiding party.[3]

The reception of undue influence in Scots law is of comparatively recent origin. A few early nineteenth century cases are sometimes referred to as evidencing the application of principles similar to those underlying undue influence,[4] but it was only really in Gray v. Binny[5] that the concept of undue influence was clearly and voluntarily accepted in Scots law. However, even at the present day the extent of its importation is uncertain.[6]

In Gray v. Binny a mother, with the help of the family solicitor, obtained from her son, who was twenty-four, a deed of consent to disentail for a grossly inadequate return, by taking advantage of the

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1 See generally W.H.D. Winder, Undue Influence in English and Scots Law (1940) 56 L.Q.R. 97.

2 Ibid.

3 Ibid., 98.

4 For example Taylor v. Long (1824) 2 Shaw 233; Ewen v. Magistrates of Montrose (1830) 4 W. & S., Sc.App. 346; Anstruther v. Wilkie (1856) 18D. 405.

5 (1879) 7R. 332.

6 See Smith, Short Commentary of the Law of Scotland, 840-841; Scottish Law Commission, Memorandum No. 42, Defective Consent and Consequential Matters, par. 3.102.

son's ignorance of his rights and by abusing the confidence that he had placed in them. The court reduced the deed on the ground of undue influence and Lord President Inglis accepted[1] the relevant principles to be those set out by the Lord Ordinary (Lord Young):

> The principle is that where a relation subsists which imports influence, together with confidence reposed, on the one side, and subjection to the influence and the giving of the confidence on the other, the Court will examine into the circumstances of any 'transaction of bounty' ... between parties so related, whereby the stronger party ... greatly benefits at the cost of the weaker, and will give relief if it appears to have been the result of influence abused or confidence betrayed.[2]

Lord Shand, in the same case, argued strongly in favour of the adoption of the principle of undue influence. He maintained that a refusal to do so would lead to

> transactions obviously unjust, entered into by one of the parties in the position of not being truly an entirely free agent, being nevertheless held valid, because it could not be shown that the deed was procured by deceit.[3]

The requirements for undue influence, Lord Shand set out as follows:

> /I/n the first place, the existence of a relation between the granter and the grantee of the deed which creates a dominant or ascendant influence, the fact that confidence and trust arose from that relation, the fact that a material and gratuitous benefit was given to the prejudice of the granter, and the circumstance that the granter entered into the transaction without the benefit of independent advice or assistance.[4]

It has been said that the essence of undue influence lies in the fact that the confiding party did not exercise a free and independent will in respect of the transaction which he concluded.[5] However,

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1 (1879) 7R.332,339.

2 Ibid., 338.

3 Ibid., 347

4 Ibid.

5 See, for example, Gray v. Binny (1879) 7R. 332, 347 per Lord Shand; Inche Noriah v. Shaik Allie Bin Omar /1929/ A.C. 127.

the ideal of the contractual party who is entirely free from outside influence is essentially unattainable. Many contracts are upheld by the courts, despite the fact that they were entered into under some outside influence. Lord Guthrie was therefore correct when he held in Forbes v. Forbes Trustees[1] that the view that the essence of undue influence was to be found in the absence of a free and independent judgment was too wide to be acceptable. Instead he approved[2] the following statement made by Lord President Clyde in Ross v. Gosselin's Executors:

> The essence of undue influence is that a person, who has assumed or undertaken a position of quasi-fiduciary responsibility in relation to the affairs of another, allows his own self-interest to deflect the advice or guidance he gives, in his own favour.[3]

The relation of confidence and trust between the parties creates a situation which enhances the opportunities for abuse. The court will, therefore, normally find undue influence if the terms of the contract itself indicate that the fiduciary relation has been abused. The tendency to judge the question of undue influence objectively, in terms of the result or effect of the transaction, rather than in terms of improper motive has been fairly consistently followed by Scottish courts.[4] What the courts regard as fair in the circumstances will ultimately depend on the institutional pattern in similar transactions and upon the mores of the community.[5] For example, the

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1 1957 S.C. 325, 331.

2 Ibid., 332.

3 1926 S.C. 325, 334.

4 See, for example, Harris v. Robertson (1864) 2 M. 664; Carmichael v. Baird 1899, 6 S.L.T. 369; McKechnie v. McKechnie's Trustees 1908 S.C. 93; Allan v. Allan and Others 1961 S.C.200.

5 M.D. Green, Fraud, Undue Influence and Mental Incompetency (1943) 43 Col.L.Rev. 176, 182, note 34.

fairness of an onerous contract is usually assessed with reference to the equality of exchange or the adequacy of consideration. When dealing with a gift or voluntary conveyance the tests for fairness are more diverse, but they still amount to an objective question, namely, whether the opportunity of abuse of influence presented by the confidential relationship has been made use of to divert the gift from its normal and natural course when seen against the background of all the relevant circumstances and the total situation of the donor - economic, social and psychological.[1]

It was implicitly accepted in Allan v. Allan and Others[2] that undue influence may be found even though the benefit arising from the transaction does not accrue to the person who exercised his influence unduly.

This does not mean that a grossly unfair transaction will not in certain circumstances receive judicial sanction. In Gray v. Binny, Lord President Inglis asserted that the contract in question would have stood if it (a) had been carried through with good advice, (b) had been concluded with careful attention to the rights of both parties, and (c) had been entered into with full knowledge on both sides.[3] However, even these tests may not be conclusive. In the same case, Lord Shand insisted that even if the son had been fully informed as to the value of the right he was renouncing he would still have regarded the transaction as having been concluded under undue influence, if

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1 J.P. Dawson, Economic Duress - An Essay in Perspective (1947) 45 Mich. L.Rev. 253, 264.

2 1961 S.C. 200, 204.

3 (1879) 7 R. 332, 340.

only because of the great prejudice which had been suffered by the son.[1] Whether he would have taken the same view even where the son had had an independent adviser, Lord Shand did not intimate. He did, however, assume that in such an event the transaction would not have been so prejudicial to the son.

> It is against all ordinary experience to suppose that if a business man or independent adviser had presented the transaction to the pursuer in the light of what was reasonable from his point of view ... that a transaction so prejudicial to himself would have followed.[2]

Despite the fact, therefore, that the concept of undue influence is generally framed in terms of motive, it is clear that the fairness of the contract terms is a very important consideration in deciding whether influence was exercised unduly or not. Nevertheless, it is evident that where the inequality caused by the one party's confidence and trust in the other, is removed, as for example, by the presence of an independent adviser, the courts will generally not intervene, no matter how prejudicial the transaction may be.

There may be circumstances in which the facts of a particular case can lead to a finding of either facility and circumvention or undue influence. In such a case both grounds may be invoked.[3]

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1 Ibid., 349.

2 Ibid. See also statement to the same effect by Lord President Inglis at page 341.

3 McKechnie v. McKechnie's Trustees 1908 S.C. 93.

6 - FORCE AND FEAR (VIS AC METUS)

Force and fear (or extortion, as it is often referred to) is derived from the Roman law of *metus*,[1] as interpreted by the medieval commentators.[2] *Metus* was fear occasioned by threats or intimidation. A person who was induced by such threats to perform damaging legal acts, such as the conveyance of property or the payment of money was given certain remedies by the *praetor*. He could defend himself by means of the *exceptio quod metus causa* or, where he had already rendered performance, claim *restitutio in integrum*. In addition, damages could be claimed with the delictual *actio quod metus causa*. The *actio* was delictual because the doctrine of *metus* arose as a supplementary incident of the criminal and delictual law against the perpetration of physical violence by private individuals.[3] The origin of the doctrine was reflected in two central requirements: Firstly, the intimidation or threat must have been one of physical violence,[4] and secondly, the threat must have been so severe as to overcome a"constant man". The transaction was reducible because it had been obtained by an unlawful act. The limited scope of *metus* was later extended by various *condictiones*, but these "left no imprint on the formal statements

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1 See generally Sohm, *Institutes of Roman Law*, 209; Buckland, *A Text-Book of Roman Law*, 593 *et seq*.

2 Scottish Law Commission Memorandum No. 42: *Defective Consent and Consequential Matters*, Vol. II, para. 3.104.

3 J.P. Dawson, Economic Duress and the Fair Exchange in French and German Law (1937) 11 Tul. L. Rev. 342, 347.

4 Sohm, *op.cit.*, 209, said only that the action threatened must have been unlawful, but Buckland, *op.cit.*, 593 insisted that it had to be a threat of physical harm.

of the doctrine in the Corpus Iuris with which medieval commentators were confronted".[1]

In dealing with the different forms of pressure which might affect the validity of an agreement the civilian legal systems generally distinguish between vis absoluta, force which leads to a physical overpowering so extreme as to exclude any question of a juristic act by the affected party, and vis compulsiva, which exists where a person is threatened with some evil unless he concludes the contract. In the former case there is no declaration of will and consequently no contract, but in the latter a contract is formed, but it is reducible at the instance of the threatened party. Bankton, who is the only institutional writer who drew this distinction clearly, rightly said of vis compulsiva that

> the fear occasioned by it does not exclude all consent. The person put in fear chuses the least of two evils, rather to part with his right, than suffer pain, or the like grievance threatened; and, as the law expresses it, Quamvis, si liberum esset, noluisset, tamen coactus voluit.[2]

Other institutional writers were more equivocal about whether force and fear excluded consent or not.[3] This has caused uncertainty as to whether a contract induced by force and fear is void ab initio or merely reducible.[4]

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1 Dawson, op.cit., 348.

2 I, 10, 50.

3 Stair, (I, 9, 8), thought that deeds or obligations extorted were valid because true consent was given. Both Erskine (III, 1, 16), and Bell (Commentaries, I,314) however, thought that consent given in such circumstances was not true, but merely apparent.

4 Gloag on Contract, 488, took the view that the effect of the institutional writing was that the agreement is void, but the Scottish Law Commission, op.cit., para. 3.115, expressed the opinion that such transactions are only voidable. See also C.M. Campbell, Force and Fear (1979) 24 J.L.S. 289.

What types of threat will found a plea of force and fear? Stair, who relied heavily on Roman law in setting out the principles of force and fear, maintained that the action threatened should be unlawful, but he clearly did not think it necessary that it should be confined to physical violence.[1] Discussing the types of threat which could possibly overcome a person of constant firmness he included "loss of estate". Bankton[2] and Bell[3] made statements to the same effect. Wiseman v. Logie[4], Foreman v. Sheriff[5] and Gow v. Henry[6] also support the proposition that a fear of economic loss caused by an unlawful threat could found a plea of force and fear. Yet, the institutional writers when they gave examples of relievable threats alluded mostly to threats of physical violence or of unlawful imprisonment. Bell, in his Commentaries, nevertheless,gave one example where even a lawful threat of imprisonment could possibly constitute legal force and fear.

> /W/henever this instrument of terror is applied to extort from a debtor something more than the debt for which imprisonment is competent, or from others advantages to which otherwise they would not have consented there seems to be such a want of lawful consent as to give relief..[7]

But, if the intimidation produced only a settlement of a debt which was due it was unlikely that a lawful threat of imprisonment would

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1 I, 9, 8.

2 I, 10, 51.

3 Principles, section 12.

4 1700 Mor. 16505.

5 1791 Mor. 16515.

6 (1899) 2F. 48 - threatened with loss of employment.

7 Commentaries, I, 315.

invalidate the transaction.[1] Bell's view that the unfairness of a transaction could lead to the invalidation of the transaction if it was entered into because of a lawful threat has received support in a few judicial dicta.[2] On the whole, however, Scots law insisted that a transaction would only be annulled on the ground of force and fear if the defender had threatened unlawful or unwarranted action.[3] This view has persisted into the twentieth century.[4]

What degree of coercion is necessary for the plea of force and fear to succeed, or when will the fear be a "just fear"? The institutional writers, although they generally followed Roman law in holding that the threat must have been such as to put a normal man in fear,[5] considerably mitigated this rule by saying that the age, sex or general weakness of a party had to be taken into account when deciding the question.[6] Stair, for example, maintained that

> extortion will be more easily presumed and sustained in the deeds of persons, who are weak and infirm of judgment or courage....than of those who are knowing and confident; and more easily in deeds and obligations gratuitous and free, than in such as are for an onerous cause, which will not easily be annulled, unlest manifest lesion do appear, or that the compulson be very evident.[7]

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1 Ibid.

2 Foreman v. Sheriff, 1791 Mor. 16515; Mackintosh v. Chalmers (1883) 11R. 8, 15; Education Authority of Dumfriesshire v. Wright 1926 S.L.T. 217.

3 Priestnell v. Hutcheson (1857) 19D. 495.

4 Hunter v. Bradford Property Trust Ltd. 1977 S.L.T. (Notes) 33. Although the judgment was only reported in 1977 it was delivered in 1957.

5 Stair, I, 9, 8; Bankton I, 10, 51; Erskine IV, 1, 26; Bell's Principles, Section 12.

6 See, for example, Bell's Principles, section 12.

7 I, 9, 8.

However, the mere fact that a person in mean circumstances conferred a benefit on a powerful party would not raise a presumption of a "just fear".[1] Despite the relaxation by the institutional writers of the strict Roman law requirement, they, and the courts,[2] still maintained that the fear should not have been "foolish or vain".[3]

Bell expressed the opinion that there was no distinction to be drawn between the case where threats were made against the person who eventually entered into the transaction and the case where the threats were directed to a near relation of his. If the other requirements were met, force and fear should be found in both cases.[4] The Scottish Law Commission has now suggested that a plea of force and fear should succeed even where a person undertakes an obligation in consequence of a threat of harm to the property or economic interests of a third party, provided that such a third party stands in a close social or economic relationship to the obligor.[5]

Despite the Roman law principle that a remedy was available even where the person receiving the benefit had not made the threat,[6] this idea has apparently not taken root in Scotland.[7] Bell[8] was the only

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1 Ibid.

2 Hunter v. Bradford Property Trust Ltd. 1977 S.L.T. (Notes) 33; Hislop v. Dickson Motors (Forres) Ltd. 1978 S.L.T. (Notes) 73.

3 Bell's Principles, section 12.

4 Ibid.

5 Op.cit., para. 3.117.

6 D. 4.2.14.3.

7 In Stewart Brothers v. Kiddie 1899, 7 S.L.T. 92, it was said that the threats had to be made by the other contractual party or by somebody on his behalf. See also Hunter v. Bradford Property Trust Ltd. 1977, S.L.T. (Notes) 33.

8 Commentaries, I, 315.

institutional writer who suggested that a remedy could lie against a third who had profited from the unlawful threat made by another. In this context the Scottish Law Commission[1] has also recommended a reform of the law so that the coerced party should have a remedy against somebody who had knowingly taken advantage of the threat made by a third person.

This short historical survey shows that even by the twentieth century little expansion of the force and fear doctrine had taken place. However, the regularity with which it was employed, especially during the seventeenth and eighteenth centuries,[2] but also in the nineteenth century indicate that even such a limited doctrine had an important function to fulfil. The lack of development might be explained by the fact that the scope of the existing doctrine was adequate to deal with the problem of compelled transactions, compulsion at that time generally taking the form of threats to life and limb. Since then, however, civil imprisonment has been abolished and the use of physical force as a form of coercion in contract law has become increasingly rare with the result that force and fear became an almost irrelevant doctrine. In the twentieth century it was increasingly realized that modern industrialised society lent itself to more sophisticated, but no less coercive forms of compulsion and in a climate in which the standards of acceptable negotiating behaviour were set ever higher there was a clear need for a re-examination of the scope of the doctrine of force

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1 Op.cit., para.3.115. Cf. the similar suggestion made in respect of English law by counsel in Barton v. Armstrong (1976) A.C. 104, 108.

2 See, for example, the cases gathered in Morison's Dictionary of Decisions, 16479 et seq.

and fear. A rare opportunity to embark upon such a re-examination came in the most recent case on force and fear, Hislop v. Dickson Motors (Forres) Ltd.[1]

In that case the pursuer, after a heated discussion, admitted embezzling some money from the defenders and agreed to repay it. As arranged the defenders called on her at home. They had with them withdrawal forms for the pursuer's savings bank account. After signing these the pursuer also handed the keys of her car to the defenders. Neither the amount embezzled nor the value of the monies or the car handed over by the pursuer was at this stage known to the parties. Having learnt, while withdrawing all the money from the pursuer's savings account, that she also had a current account, the defenders returned to the pursuer's home. After some hectoring the pursuer gave the defenders a blank cheque which they subsequently cashed to the amount in credit. The pursuer averred that she was compelled by force and fear to sign the withdrawal form and the cheque, which were, therefore, not voluntary deeds by her and that the car was taken from her without any consent whether voluntary or otherwise. In support of this contention the pursuer relied on the defenders' threats to report her to the police for alleged embezzlement and maintained that these, coupled with the consequent fear of prosecution and damage to reputation, amounted to an unlawful threat.

The Lord Ordinary (Lord Maxwell) drew a distinction between threats and the exercise of pressure and held that the only threat

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1 1978 S.L.T. (Notes) 73, discussed by Campbell, op.cit.

actually proved was not a threat in the sense in which the word is used in extortion cases:

> The characteristic of such a threat is the expression or implication of intention to do something, as for example to report to the police, unless the victim gives way to the extortioner's demand.[1]

In this case there was no such implication of "buying off" of the action threatened. And in any case, the Lord Ordinary added, a threat to report to the police was not illegal or unwarrantable. Lord Maxwell did, however, indicate that a threatened action, even if it was not unlawful might found a plea of extortion where it was not "used in good faith to get back that which is due in respect of the matter with regard to which the threat is made". In applying this test his Lordship found the English authorities to be an unsafe guide as they seemed to have moved more in favour of the party claiming reduction than the Scots cases and because of the different bases of prosecution in the two jurisdictions. Although little indication was given it would seem as if a threat which was otherwise lawful would be used in bad faith if it was made to induce payment of more money than was in fact due or where the threat of legal proceedings was used in order to apply pressure in a matter unconnected with the subject-matter of the proceedings.

Lord Maxwell also expressed the opinion that apart from threats which might affect the validity of a contract

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[1] Ibid., 74-75.

> there is a broader underlying principle that deeds will be reducible and payments recoverable when they have been extracted by pressure of a certain degree. In general the pressure must be such as would overpower the mind of a person of ordinary firmness so that there is no true consent.[1]

Despite finding that there was no such threat as would render a contract reducible, Lord Maxwell ordered repayment of the sum extracted from the plaintiff by cheque and declared:

> I am of the opinion that against the whole background and in the light of the sudden reappearance of the Dickson brothers, armed with knowledge of an account which the pursuer had never volunteered and demanding that she admit the truth, the action of the pursuer in signing a blank cheque cannot reasonably be considered a truly voluntary act on her part, but was rather the submission to pressure which might in the whole circumstance well have overpowered the mind of a woman of normal firmness finding herself in such a situation. While the pursuer in fact signed the cheque, I consider that the abstraction by the defender of the funds in her account is more akin to a forceful seizure of those funds than a voluntary payment of them by her.[2]

Lord Maxwell's decision that conduct which was not normally unlawful might in certain circumstances be wrongful if used oppressively or for the purpose of inducing another person to perform some transaction, constituted a very welcome extension of the force and fear doctrine. Together with the notion, hinted at by some of the institutional writers, that threats aimed at the economic interests of a party could cause a just fear, it should open the way towards the greater regulation of lawful, but nevertheless oppressive, economic compulsion. It is a pity that the judicial innovation was not

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1 Ibid., 75.

2 Ibid., 76-77.

accompanied by a greater attempt at elucidation, because the judgment also raised a number of problems.

As I have indicated before, the Lord Ordinary distinguished between fear resulting from threats and imprisonment on the one hand, and "pressure" on the other. Although the judge thought that threats implied a "buying off", the distinction was not further clarified and there would seem little merit in differentiating between the various forms of compulsion on that basis. Lord Maxwell did say that in the case of threats and actual imprisonment "the requirement of the overpowering of the mind of reasonable firmness has been somewhat departed from...but in other cases in my opinion it is still the law".[1] Where, therefore, a contract was concluded under "pressure" it would still be necessary to prove that the pressure was such as to overcome a reasonably constant person so that there was no "true consent". This formulation raises various problematic issues, not the least of which is the difficult psychological distinctions as to when the mind of a person will be so overcome by fear that he cannot be said to have given true consent and when not. The judgment in the Hislop case provided no criteria for the drawing of this distinction. Secondly, there is the contention by various commentators already referred to in the discussion on duress,[2] that it is inaccurate and unhelpful to assume the absence of consent where such consent was induced by compulsion. Thirdly, there is the acceptance by Lord Maxwell of the

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1 Ibid., 76.

2 Ante, 167.

constant firmness test. If the absence of true consent is the fundamental question on which reducibility depends then surely the test should be wholly subjective. A coercing party should not be able to defend the transaction by saying that the coerced person should not have been coerced so easily. A party must be held responsible for the consequences which he intended and where the very aim of exerting the pressure was to coerce an otherwise unwilling party into contracting, reduction should not be prevented merely because a reasonably constant person would not have succumbed to it. The question of the reasonableness of the fear should, nevertheless, be an evidentiary factor in deciding whether a person was in fact coerced.

The relationship between force and fear and the fairness of the coerced transaction

In Roman law metus arose to provide remedies to a person who had performed damaging or disadvantageous acts as a result of unlawful intimidation. The same concern over the damage suffered by the coerced party was translated into the doctrine of force and fear. Throughout its history great emphasis has been placed on the fairness of the transaction induced by the coercion. Most of the cases that have come before the courts have been claims for the restitution of transfers or payments made in settlement of debts that were not in fact owed or where the actual debt was smaller than the amount paid. On the one hand, the courts have been prepared to uphold payments obtained by unlawful intimidation where the payment was in fact owed;[1]

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[1] See, for example, Foreman v. Sheriff, 1791 Mor. 16515, where the court seemed prepared to uphold the payment upon proof that the sum paid was not exorbitant.

on the other, they have been prepared to give relief where a conveyance had been made or money paid in consequence of a lawful threat if the property conveyed or money paid exceeded any debt owed.[1] The merits of the transaction have therefore played an important role in the extension of force and fear.

In addition, there is the authority of Stair[2] and Bankton[3] in support of the proposition that extortion would be more easily assumed in gratuitous deeds and obligations, or in the case of onerous deeds, where there was manifest lesion. Where, however, "the compulsion /was/ very evident"[4] policy dictated the award of a remedy even where the lesion was not so great.

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1 Ante, 226-227.

2 I, 9, 8.

3 I, 10, 51.

4 Stair, I, 9, 8.

7 - IRRITANCY PROVISIONS

An irritancy clause confers on the party in whose favour it has been drafted, the right to terminate or cancel the contract on the occurrence of some event on which the operation of the clause has been made dependent. Irritancy clauses are sometimes distinguished from penalties by the fact that under the former, the party in default merely loses his rights under the contract, whereas under the latter, the party in breach forfeits property to which he has an independent title.[1]

Irritancies may be either legal, that is of a type which the law generally implies in contracts of a particular kind, or conventional, that is agreed upon by the parties and expressly inserted in the contract.[2] Irritancy provisions are most frequently found in feu contracts and leases, but they are not confined to these contracts.[3] It is common in leases or feu contracts to stipulate for an irritancy in the event of the insolvency or bankruptcy of the tenant or feuar, or on his failure to pay the rent or the feu duty.[4]

In the seventeenth and eighteenth centuries leases or tacks were regarded as contracts _stricti iuris_, to be enforced strictly according to the terms in which they were expressed.[5] As irritancies

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1 See, for example, Smith, _Short Commentary on the Law of Scotland_, 856; Gloag on _Contract_, 664.

2 Gloag, _op. cit._, 665; Walker, _The Law of Civil Remedies in Scotland_, 85-87.

3 Walker, _op. cit._, 85.

4 Gloag, _op. cit._, 665.

5 Stair II, 9, 26; Bankton II, 9, 11; Erskine II, 6, 31.

were, during that time, mostly found in tacks it followed that they too were enforced according to the letter. The practice of interpreting irritancies strictly soon hardened into a general rule applied irrespective of the contracts in which they were contained. Even at the present day, irritancies are enforced without any regard to the hardship which it may cause.[1]

In the case of legal irritancies the strict rule is mitigated by the fact that the party in default may "purge" it, for example, by payment of the rent or the feu duty, before the decree passes in an action for enforcement of the irritancy.[2] Whether purgation is possible in the case of conventional irritancies is a more controversial question. On the one hand, it is generally accepted that irritancies in feu contracts may be purged irrespective of whether they are legal or conventional.[3] On the other hand, the nineteenth century case of Stewart v. Watson[4] is usually cited as having authoritatively settled the law in relation to all other conventional irritancies in favour of non-purgation. The decision in that case was followed in M'Douall's Trustees v. MacLeod[5] and recently affirmed by the House of Lords in Dorchester Studios (Glasgow) Ltd. v. Stone and Another.[6] The strict rule that conventional irritancies cannot be purged and that effect should be given to the provision irrespective of whether the party in

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1 Gloag, op. cit., 665; Dorchester Studios (Glasgow) Ltd. v. Stone and Another 1975 S.L.T. (H.L.) 153, 157.

2 Walker, op. cit., 89; Dorchester Studios (Glasgow) Ltd. v. Stone and Another, supra.

3 Ibid.

4 (1864) 2 M. 1414.

5 1949 S.C. 593.

6 1975 S.L.T. (H.L.) 153.

default is willing and able to purge or that the party in whose favour the irritancy was inserted, suffers little or no loss through such purgation, stands in stark contrast to the treatment in English law of forfeiture clauses in leases.[1] This harsh rule, which is largely the result of judicial rigidity in the nineteenth century, has been subjected to strong criticism.[2]

Pre-nineteenth century law

In the seventeenth and eighteenth centuries the rule that irritancies were to be enforced strictly was mitigated by distinguishing between penal and non-penal irritancies. Non-penal irritancies were enforced without giving any opportunity for purgation, but a penal irritancy, which required a declarator of the court before being enforced, could be purged. According to Stair the Lords

> ... have power to qualify these clauses irritant, and to allow time for purging the same; yet only if they be truly exorbitantly penal: for such clauses contained in gratuitous rights take their full effect, because then they are not penal, but are conditions and provisions qualifying the right.[3]

The caselaw of this period, which was extensively surveyed in both the M'Douall's Trustees[4] and Dorchester Studios[5] cases, is contradictory and because the reasons for a court's decision are seldom given, it is

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1 Ante, 33.

2 See, for example, Dorchester Studios (Glasgow) Ltd. v. Stone and Another 1975 S.L.T. (H.L.) 153, 156 per Lord Kilbrandon; Irritancy in Leases (1976) 21 J.L.S.4; W.W. McBryde, Breach of Contract (1979) 24 Jur.Rev. 60-63.

3 IV, 18, 3. See also Stair I, 10, 14 and Erskine II, 8, 14.

4 1949 S.C. 593, 600-601 per Lord Justice-Clerk Thomson and at 611-614 per Lord Mackay.

5 1975 S.L.T. (H.L.) 153, 157-158 per Lord Fraser of Tullybelton.

difficult to establish the grounds on which the courts proceed. It was, nevertheless, considered penal that a feuar should lose the whole estate simply because he had omitted to pay a term's rent and he was therefore given the opportunity to purge his default.[1] On the other hand, a similar irritancy in a lease, which if enforced would have resulted only in the landlord getting his own property back, was generally not regarded as penal and could therefore not be purged.[2] At the same time, however, some cases did allow purgation of irritancies in leases.[3] It would seem as if the courts were reluctant to enforce an irritancy clause if the contractual obligation which the clause fenced was complied with, in whatever way, so that the irritancy had in effect fulfilled its purpose.[4] However, despite the uncertain picture presented by the case law of that time an early nineteenth century writer on the law of leases still declared that whatever might have been the position earlier, irritancies in leases whether legal or conventional, were then purgeable at any time before a decree in foro was made.[5]

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1 Hepburn v. Nisbet 1665 Mor. 7229.

2 Hay v. Moffat 1586 Mor. 7226; George Seton v. James Seton 1611 Mor. 7184; Finlayson and Weir v. Clayton 1761 Mor. 7239; Clerk v. Bennet 1759 Mor. 7237.

3 Bishop of Orkney v. Sinclair 1587 Mor. 7227; Old College of Aberdeen v. Earl of Northesk 1675 Mor. 7230; Hogg v. Hogg (1780) 2 Paton App. 516.

4 See, for example, Forsyth and Johnston v. Kennedy 1708 Mor. 7255 where an irritancy for sub-letting was held purgeable because the sub-letting had terminated by the time the landlord wished to enforce the irritancy. Also Hog v. Morton (1825) 35. 617 where the court refused to allow the landlord to irritate the lease as the arrears in the rent had been extinguished by the landlord sequestrating the stock and selling it.

5 Bell, Treatise on Leases, 184-185. See also Gloag, op. cit., 666.

The nineteenth and twentieth centuries

During the nineteenth century the already rigid distinction between conventional irritancies in feus - which the courts generally regarded as penal because they involved the loss of property - and irritancies in leases - which were ordinarily thought of as non-penal - was applied without considering the reason underlying it.[1] It consequently became firmly established that conventional irritancies in feu contracts could be purged, but that purgation was impossible in the case of irritancies in leases.[2] The notion that leases, unlike feus, do not convey a right of property was questioned by Lord Kilbrandon in the Dorchester Studios case and described as wearing "today an air of unreality".[3]

To the nineteenth century judges, two considerations, in particular, militated in favour of holding conventional irritancies, other than those contained in feus, non-purgeable. The first, and most important, was that a conventional irritancy was expressly included in a consensual contract and should therefore be taken to be an expression of the intention of the parties. It followed from the elevated status accorded to the parties' intention in nineteenth century contract theory that such irritancies should be given effect to irrespective of their fairness.[4] As Lord Justice-Clerk Inglis said in Stewart v. Watson: "An intending tenant may or may not agree to such a stipulation, but if he does, I think there is no doubt that he

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1 Stewart v. Watson (1864) 2M. 1414, 1416, 1422.

2 Ibid. See also Lyon v. Irvine (1874) 1R. 512, 518.

3 1975 S.L.T. 153, 156.

4 See, for example, M'Douall's Trustees v. MacLeod 1949 S.C. 593, 604.

must be bound by it."[1] And Lord Neaves declared: "I am of the same opinion. In all consensual contracts the agreements of parties ought to be enforced."[2] These sentiments were enthusiastically approved almost a century later in M'Douall's Trustees v. MacLeod[3] and received a similarly sympathetic reception from Lord Fraser of Tullybelton in Dorchester Studios(Glasgow) Ltd. v. Stone and Another. His Lordship maintained that "if the tenant has agreed to a lease containing an irritancy I do not think it is in principle unfair to hold him to his bargain"[4] even if he were only one day late in paying his rent.

In the second place, irritancies were in the nineteenth century increasingly regarded not as a means whereby enforcement of a contractual obligation could be effected, but as a method by which a landlord could rid himself of an unsatisfactory tenant,[5] and this view has been carried through to the twentieth century. In M'Douall's Trustees, Lord Mackay described[6] the following dictum, by Lord Kinnear in Cassels v. Lamb,[7] as not applicable to leases. His Lordship, discussing the power of the court to allow purgation of an irritancy, had said:

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1 (1864) 2 M. 1414, 1420.

2 Ibid., 1422.

3 1949 S.C. 593, 604 per Lord Mackay.

4 1975 S.L.T. (H.L.) 153, 159.

5 Stewart v. Watson (1864) 2M. 1414, 1420.

6 1949 S.C. 593, 610.

7 (1885) 12R, 722.

> /T/he true ground of this equitable interference, in violation of the letter of a clause of irritancy, is, that in substance the condition is a stringent remedy for non-payment or non-performance. The Court, therefore, interferes to carry out the true intention of the contract, by allowing the irritancy to be purged when its purpose of compelling performance has been effectuated.[1]

In Dorchester Studios, Lord Fraser thought it not unreasonable that a landlord might rely on an irritancy to get rid of an unsatisfactory tenant,[2] but Lord Kilbrandon questioned whether a doctrine founded upon such a purpose reflected current social policy.[3]

Purgation on the ground of oppression

Despite general judicial approbation of the modern rule that conventional irritancies may not be purged, it has been repeatedly stated that the Court of Session retains a residual power to allow time for purgation if the irritancy provision is abused or used oppressively.[4] However, it has been said that the court will only "violate the terms of the bargain, if there are circumstances of extreme abuse or heavy equities."[5] The equitable power has not been applied in any modern case and it is uncertain in which circumstances it will be exercised. In Lucas's Executors v. Demarco[6] Lord Guthrie said:

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1 Ibid., 777.

2 1975 S.L.T. (H.L.) 153, 159.

3 Ibid., 156.

4 Stewart v. Watson (1864) 2M. 1414; Dorchester Studios(Glasgow) Ltd. v. Stone and Another 1975 S.L.T. (H.L.) 153.

5 M'Douall's Trustees v. MacLeod 1949 S.C. 593, 607 per Lord Mackay.

6 1968 S.L.T. 89.

> 'Oppression' infers that there has been impropriety of conduct on the part of the landlords. 'Misuse of rights' or 'abuse of irritancies' involves that the terms of the contract have been invoked by the landlord to procure an unfair consequence to the tenant.[1]

But in the same case Lord President Clyde cited[2] with approval the following dictum of Lord Chancellor Birkenhead in Gatty v. Maclaine:

> It would, in my opinion, be quite wrong and it is certainly without justification in authority for a court of law to deprive parties of their clear contractual rights by a consideration of possible motives or prejudices which the party in default may suffer if the contract is enforced.[3]

It is clear that the courts' equitable power to allow purgation has been interpreted so restrictively that it is doubtful whether there remain many realistic circumstances in which it can meaningfully be brought to bear.[4]

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1 Ibid., 96.

2 Ibid., 95.

3 1921 S.C. (H.L.) 1, 6.

4 See Irritancy in Leases (1976) 21 J.L.S. 4, 5-6.

C - ENGLISH AND SCOTS LAW

1 - MANIPULATION OF THE RULES OF CONSENT

Unfair contract terms, particularly exemption clauses, are usually contained in printed documents. The courts soon realised that the notion of consent gave them a lever which could be manipulated against such terms. A party who wishes to rely on a particular term first has to show that it has been incorporated into the contract.

(i) Signature

It was decided in L'Estrange v. F. Graucob[1] that where a contractual document has been signed by a party, he is bound by the terms contained in it, notwithstanding the fact that he may never have read them. The injustice of this long standing rule has been widely recognised[2] and attempts have been made to ameliorate its effects. In the Canadian case of Tilden Rent-a-Car v. Clendenning[3] the court held that a signature could only be relied on as manifesting consent if the party who was relying on the signed document could reasonably have believed that the signer did consent to all the terms contained in the document. Where a contract was concluded in a hurry the offeror of the document could not reasonably draw such an inference and was therefore precluded from relying on any onerous or unusual printed

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1 /1934/ 2 K.B. 394; Bahamas Oil Refining Co. v. Kristiansands Tankrederie A/S /1978/ 1 Ll. Rep. 211, 215-216.

2 McCutcheon v. David MacBrayne Ltd. /1964/ 1 W.L.R. 125, 133 per Lord Devlin. See also the remarks made by Lord Denning M.R. in (1967) 41 Aus. L.J. 261, 268-269; J.R. Spencer, Signature, Consent, and the Rule in L'Estrange v. Graucob (1973) C.L.J. 104.

3 (1978) 83 D.L.R. (3d) 400.

terms not specifically drawn to the attention of the signer.[1]

It has also been decided that where the offeror of a document (or his agent) misrepresented the effect of its terms, he is deprived of the benefits conveyed by such terms notwithstanding the fact that the document had been signed. In Curtis v. Chemical Cleaning & Dyeing Co. Ltd.,[2] Denning L.J. declared that in certain circumstances even a mere failure to draw attention to the existence of an exemption clause might amount to sufficient misrepresentation.

(ii) Notice

The greatest activity of the courts has, however, been in those cases where there was no incriminating signature and the terms on which the offeror was relying were contained in a printed document which was either handed to the offeree or displayed in a central place. Here a detailed set of rules has developed, the effect of which has been to lay down strict limitations to the incorporation into the contract of unsigned documents.

In order to qualify for incorporation a document containing an exemption clause must have special significance as a contractual document. The question of what falls within that category has been approached strictly. Notwithstanding a long line of carriage and deposit cases recognising "tickets" as contractual documents, the courts have been loath to expand this category. In Taylor v. Glasgow

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1 Ibid., 405-410 per Dubin J.A. See also Jaques v. Lloyd D. George & Partners Ltd. [1968] 1 W.L.R. 625.

2 [1951] 1 K.B. 805, 809.

Corporation[1] the Court of Session decided that a ticket handed to a person wishing to use a public bath was not to be regarded as a contractual document, but was a mere voucher or receipt. An exemption clause contained in a ticket for the hire of a deck chair has similarly been held to be ineffective.[2] There can be no doubt that the reluctance to enlarge the category of "contractual" documents is based on a policy against unfair exemption clauses.

Once it has been decided that a document has contractual force the courts may further limit the incorporation of the terms by the degree of notice which they require. In Parker v. South Eastern Railway,[3] Mellish L.J. stated that in order to incorporate a document, the party to whom it is given must have been aware of the terms contained in it, or that it must have been handed to him in such a way that a reasonable man would have concluded that it contained contractual terms.[4] The adequacy of the steps taken to bring the terms to the notice of the offeree might also depend upon whether the offeror knew, or should have known, that the offeree suffered from a disability which would have precluded him from gaining knowledge of the printed terms. Where, for example, the offeree was illiterate[5] or could not understand

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1 1952 S.C. 440.

2 Chapelton v. Barry U.D.C. /1940/ 1 K.B. 532. See also Jude v. Edinburgh Corporation 1943 S.C. 399; The Eagle /1977/2 Ll. Rep. 70.

3 (1877) 2 C.P.D. 416, 423.

4 See also Lewis v. Laird Line 1925 S.L.T. 316; Williamson v. North of Scotland and Orkney and Shetland Steam Navigation Co. 1916 S.C. 554; Caven v. Scottish and Universal Newspapers 1976 S.L.T. 92; Henderson v. Stevenson 1875 2R. 71 (H.L.)

5 Richardson, Spence & Co. v. Rowntree /1894/ A.C. 217 (H.L.) Cf., Thompson v. L.M. & S. Railway /1930/ 1 K.B. 41.

the language[1] in which the terms were expressed a higher degree of notice would be required for incorporation.

The degree of notice required for a successful incorporation of a document is a flexible mechanism which is also used for protecting a party against the workings of an unusual clause. In Thornton v. Shoe Lane Parking,[2] Megaw L.J. held that where a restrictive condition is "usual" it will be sufficient if the party has received "fair" notice that "some" conditions are intended to become part of the contract. Where, however, the conditions are not usual in that type of contract, it must be shown that the notice was fair in relation to conditions of that particular type.[3] The sufficiency of notice will thus depend upon whether it was fair to hold the offeree bound by the restrictive condition in the circumstances of the case. In J. Spurling Ltd. v. Bradshaw,[4] Denning L.J. also declared that the more unreasonable a term, the greater was the notice which was required to be given, and he added:

> Some clauses which I have seen would need to be printed in red ink on the face of the document with a red hand pointing to it before the notice could be held to be sufficient.[5]

Another technique often employed by the courts is to hold that terms must be brought to the attention of the party either before contracting or contemporaneously with the conclusion of the contract.

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1 Geier v. Kujawa, Weston and Warne Bros (Transport) Ltd. [1970] 1 Ll. Rep. 365, 368.

2 [1971] 2 Q.B. 163.

3 Ibid., 172.

4 [1956] 1 W.L.R. 461.

5 Ibid., 466.

Thus in Olley v. Marlborough Court Ltd.,[1] a notice in a hotel bedroom purporting to exempt the proprietors from liability for the loss of the guests' luggage was held not to be incorporated as the contract had been concluded earlier, at the reception desk.

Another instance where the courts refuse to give effect to a printed exemption clause is where a separate oral warranty is taken to override the exclusion clause. In Couchman v. Hill[2] the plaintiff, at an auction, bought a heifer described in the catalogue as "unserved". The catalogue also set out the usual conditions of sale and stated inter alia that lots must be taken subject to error of description. At the sale the plaintiff asked both the defendant and the auctioneer whether the heifer was in fact unserved, to which they replied in the affirmative. When the heifer died as a result of being in calf the plaintiff claimed damages for breach of warranty. Scott L.J. held that the defendant could not rely on the exemption clause contained in the catalogue, because by answering plaintiff's question in the affirmative he had made an offer of a warranty to plaintiff which overrode the printed conditions. This offer was accepted when the lot was knocked down to the plaintiff.[3]

Exemption clauses can be incorporated into a contract on the basis of a course of dealing but here too the requirements are stringent.

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1 [1949] 1 K.B. 532. See also Macrae v. K.I. Limited 1962 S.L.T. (Notes) 90; The Eagle [1977] 2 Ll. Rep. 70.

2 [1947] K.B. 554.

3 See also Harling v. Eddy [1951] 2 K.B. 739; Webster v. Higgins [1948] 2 All E.R. 127; Mendelssohn v. Normand Ltd. [1970] 1 Q.B. 177; Gallaher Ltd. v. B.R.S. Ltd. and Containerway & Roadferry Ltd. [1974] 2 Ll. Rep. 440; J. Evans & Son (Portsmouth) Ltd. v. Andrea Merzario Ltd. [1976] 1 W.L.R. 1078, 1081-1082.

In McCutcheon v. David MacBrayne,[1] the pursuer's agent, on account of an oversight by the defender, was not asked to sign a "three or four thousand" word document containing amongst others, a clause protecting the carrier from all "loss.... wheresoever or whensoever occurring". Lord Devlin, in holding that the clause had not been incorporated into the contract, stated that "previous dealings are relevant only if they prove knowledge of the terms, actual and not constructive, and assent to them".[2] Here the pursuer had no knowledge of the purport of the conditions. The requirement of actual knowledge has now been overruled by the House of Lords.[3]

The Court of Appeal has decided in Hollier v. Rambler Motors (AMC) Ltd.,[4] that three or four transactions over a period of five years do not constitute a course of dealing sufficient to incorporate an exempting provision. In British Crane Hire v. Ipswich Plant Hire[5] there were only two prior dealings and they occurred a long time before. It would thus not have been very realistic to speak of a course of dealing in that case. Nevertheless, Lord Denning M.R. maintained that the exempting conditions were incorporated into the contract on the basis of a "common understanding".[6] He contrasted this case with that of Hollier v. Rambler Motors (AMC) Ltd., and said:

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1 [1964] 1 W.L.R. 125.

2 Ibid., 134.

3 Hardwick Game Farm v. Suffolk Agricultural Poultry Producers Association [1969] 2 A.C. 31, 90.

4 [1972] 1 All E.R. 399.

5 [1975] Q.B. 303. See also Grayston Plant v. Plean Precast 1976 S.C.206.

6 Ibid., 311.

> That was a case of a private individual....The plaintiff there was not of equal bargaining power... The conditions were not incorporated. But here the parties were both in the trade and were of equal bargaining power.[1]

The courts have used the rules of consent very effectively to exclude from contracts such standard terms as had not been properly brought to the notice of the other party. However, such remedial action by the courts can at most be supplementary. As Lord Devlin said in McCutcheon v. David MacBrayne Ltd.,[2] such standardized terms are seldom read by the parties at whom they are directed and, indeed, are not intended to be read by them. In addition, the mere fact that certain terms were brought to the notice of a contracting party is of no assistance to him if they are not negotiable or where alternative terms are not available. While, therefore, the rules of consent as developed by the courts to limit the incorporation of standardized terms may alleviate the position, they are inadequate in themselves to solve the problems thrown up by the use of standard form contracts.

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1 Ibid., 310.

2 [1964] 1 W.L.R. 125, 133.

2 - INTERPRETATION/CONSTRUCTION OF CONTRACT[1]

Once it has been established that an exemption clause was incorporated into a standard form contract the courts may further limit its effect by construing it very narrowly. An Australian judge has even promised that the courts would use the rules of construction in such a way as to "read out" or "read down" unfair exemption clauses.[2] Construction has indeed been the main technique used to ameliorate the effect of harsh terms in contracts. The advantage of the construction method is that an objectionable clause can be excised from the contract without necessarily bringing the whole contract to an end. The doctrine of fundamental breach which has been described by the House of Lords as based essentially on the rules of construction will be discussed in the following section.

(i) The contra proferentem rule

The principal rule of construction in respect of exemption clauses is that in order to be effective in the way intended by their drafters they must be expressed in clear and unambiguous words.[3] It has even been stated by Lord Wilberforce that the more radical the breach the clearer the language of the exemption clause must be to

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1 See generally E.W. Patterson, The Interpretation and Construction of Contracts (1964) 64 Col. L. Rev. 833; Treitel, Law of Contract, 157-160. Also E.A. Farnsworth, "Meaning" in the Law of Contracts (1967) 76 Yale L.J. 939.

2 C.H. Bright, Contracts of Adhesion and Exemption Clauses (1967) 41 Aus. L.J. 261, 263.

3 Hamilton v. The Western Bank of Scotland (1861) 23D. 1033, 1037; Stevenson v. Henderson (1873) 1R. 215, 221.

free the party in breach from liability.[1] When there is any ambiguity in the clause it will be construed adversely or contra proferentem, that is, unfavourably against the drafter of the clause who is relying on it (the proferens) and favourably towards the other party. This canon of construction is widely followed in both Scots and English law. Thus a declaration, made in connection with an insurance policy, to the effect that a party was a total abstainer from alcoholic drinks and had been since birth, was held not to cover future behaviour,[2] and in F.S. Stowell, Ltd. v. Nicholls and Co. (Brighton) Ltd.[3] a clause limiting liability for loss or damage to goods to "£200 per ton of the gross weight" was construed as £200 per ton or part of a ton and not £200 per ton gross weight pro rata, as the defendants had contended. And in John Lee and Son (Grantham) Ltd. v. Railway Executive,[4] where a clause in a lease purported to exclude liability for loss or damage (whether by act or neglect of the company or their servants or agents or not) "which but for the tenancy hereby created or anything done pursuant to the provisions hereof would not have arisen", Sir Raymond Evershed M.R. found that the phrase "which....arisen" confined the exemption to liability created by the lease relationship. The contra proferentem rule applied here, he said, otherwise the clause would be extravagantly wide.[5]

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1 Suisse Atlantique Societe d'Armement Maritime S.A. v. N.V. Rotterdamsche Kolen Centrale (1967) 1 A.C. 361, 432. [This case will hereafter be referred to as Suisse Atlantique.]

2 Kennedy v. Smith and Ansvar Insurance Co. Ltd. 1976 S.L.T. 110.

3 [1963] 2 Ll. Rep. 275.

4 [1949] 2 All E.R. 581.

5 Ibid., 582-583.

In England, application of the contra proferentem rule also has the effect that a clause which specifically excluded warranties would not necessarily exclude liability for breach of conditions,[1] or that a clause which gave protection for breach of implied conditions and warranties would not afford protection if the party breached an express provision of the contract.[2]

Contra proferentem construction is used not only where exemption clauses are concerned. In Aitken's Trustees v. Bank of Scotland[3] it was, for example, also applied in the construction of a formal guarantee given by a cautioner.[4]

(ii) Exemption or Indemnity[5] from liability for negligence

The validity of clauses purporting to exempt a party from liability for negligence will be severely curtailed by the provisions of the Unfair Contract Terms Act 1977.[6] However, the effectiveness of such clauses

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1 Wallis, Son & Wells v. Pratt & Haynes /1911/ A.C. 394.

2 Andrews Bros. (Bournemouth) Ltd. v. Singer and Co. Ltd. /1934/ 1 K.B. 17.

3 1944 S.C. 270.

4 In respect of contra proferentem construction see also: Robert Hutchison and Co. Ltd. v. British Railway Board 1970 S.L.T. (Notes) 72; Kyle v. East Kilbride Town Council 1970 S.L.T. (Sh. Ct.)37; North of Scotland Hydro-Electric Board v. D. & R. Taylor 1956 S.C. 1.

5 In Smith v. U.B.M. Chrysler (Scotland) and South Wales Switchgear Co. Ltd. 1978 S.L.T. 21, 29, Lord Fraser of Tullybelton thought that the rules which had been developed in respect of clauses excluding liability for negligence similarly applied where a clause stipulated for the indemnifying of a party from liability for negligence.

6 Sections 2 and 16.

had become severely limited as a result of particularly narrow construction by the courts long before the passing of that Act. According to Buckley L.J. the reason for this practice was that the courts regarded it as "inherently improbable that one party to a contract should intend to absolve the other party from the consequences of the latter's own negligence."[1] It has, therefore, been held that a clause exempting a party from liability for breach will not be given effect to unless "adequate"[2] words were used. But the matter does not end there.

A distinction has further been drawn between cases where there are heads of damage other than that caused by negligence for which a party can be held liable and those where he can only be liable for negligence. Where a party in breach can be held liable irrespective of negligence, the courts will generally construe the exemption clause as not excluding liability for damage caused by negligence.[3] In order to protect a party from liability under such circumstances very clear words will have to be used in the exemption clause. This requirement is usually fulfilled when the words indicate that liability for all loss or damage, no matter how it might arise, is covered by the exemption clause, for example, "any cause whatever"[4] or "at customer's sole

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1 Gillespie Bros. Ltd. v. Roy Bowles Transport Ltd. /1973/ Q.B. 400, 419.

2 Rutter v. Palmer /1922/ 2 K.B. 87, 92 per Scrutton L.J.

3 North of Scotland Hydro-Electric Board v. D. & R. Taylor 1956 S.C.1; Canada Steamship Lines Ltd. v. R. /1952/ A.C. 192; White v. J. Warrick & Co., Ltd. /1953/ 2 All E.R. 1021.

4 Rutter v. Palmer /1922/2 K.B. 87, 94 per Atkin L.J.

risk".[1] However, the courts' result-oriented construction makes it extremely difficult to forecast with certainty which clauses will be adequately worded so as to exclude liability for negligence. In a recent case the phrase "all loss or damage whatsoever"[2] was construed as not covering liability for damage caused by negligence.

Where, however, liability for negligence is the only possible head of damage to which an exemption clause can apply then the clause will operate more readily to exempt the party.[3] In Alderslade v. Hendon Laundry Ltd.,[4] the defendant, having negligently lost articles belonging to the plaintiff, wished to rely on a clause stating: "The maximum amount allowed for lost or damaged articles twenty times the charge for laundering". Lord Greene M.R. held that as the only liability that could realistically arise was for negligence or default the clause had to be construed as pertaining to negligence, otherwise it would have been devoid of subject-matter.[5]

However, it does not axiomatically follow from the fact that a party can only be liable for negligence, that an exemption clause will necessarily exclude him from liability. In Hollier v. Rambler Motors (A.M.C.) Ltd.,[6] Salmon L.J. was called upon to construe a clause

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1 Ibid.

2 Smith v. U.B.M. Chrysler (Scotland) and South Wales Switchgear Co. Ltd. 1978 S.L.T. 21.

3 Rutter v. Palmer [1922] 2 K.B. 87, 92 per Scrutton L.J.

4 [1945] 1 K.B. 189.

5 Ibid., 192.

6 [1972] 1 All E.R. 399.

which read: "The company is not responsible for damage caused by fire to customers' cars on the premises". His Lordship reasoned, rather unconvincingly, that because ordinary people, confronted by such a clause, would interpret it as excluding liability only for damage not due to the negligence of the defendant, the clause was ineffective where the fire was in fact caused by the defendant's negligence. It is clear that even where a party's liability can only be for negligence, a clause will only exempt him if it is expressed in words which clearly encompass such a contingency.

(iii) Repugnancy

Although more frequently used in connection with deeds than contracts the doctrine of repugnancy may also function to deprive an objectionable clause of effect. This can occur where a party gives a positive promise to perform something which is then rendered illusory by another clause nullifying the effect of the first.[1] As Devlin J. expressed it in Firestone Tyre and Rubber Co. Ltd. v. Vokins; "It is illusory to say: 'We promise to do a thing but we are not liable if we do not do it.'"[2] The underlying fear seems to be that the contract will be reduced to a mere declaration of intent. The repugnancy doctrine may also operate where, in a contractual document, a written clause contradicts a printed one. In such a case the written terms will

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1 See generally Adams v. Richardson and Starling Ltd. [1969] 2 All E.R. 1221, 1224 per Lord Denning M.R. (dissenting); N.F. Lanitis & Co. Ltd. v. Kyodo Shoji (U.K.) Ltd. [1956] 2 Ll. Rep. 176, 178-179.

2 [1951] 1 Ll. Rep. 32, 39.

prevail, presumably because the latter will more closely correspond with the real intentions of the parties.[1]

This survey indicates that the control over the volitions of contractual parties by means of various rules of construction has been extensive. The process of policy-orientated construction has been well described by Lord Denning M.R. in Gillespie Bros. and Co. Ltd. v. Roy Bowles Transport Ltd:

> But, even so, I say to myself: This indemnity clause, in its ordinary meaning, is wide enough to cover the negligence of the carrier himself. Why should not effect be given to it? What is the justification for the courts, in this or any other case, departing from the ordinary meaning of the words? If you examine all the cases, you will, I think, find that at bottom it is because the clause (relieving a man from his own negligence) is unreasonable, or is being applied unreasonably in the circumstances of the particular case. The judges have, then, time after time, sanctioned a departure from the ordinary meaning. They have done it under the guise of "construing" the clause. They assume that the party cannot have intended anything so unreasonable. So they construe the clause "strictly". They cut down the ordinary meaning of the words and reduce them to reasonable proportions. They use all their skill and art to this end... I know that the judges hitherto have never confessed openly to the test of reasonableness. But it has been the driving force behind many of the decisions".[2]

Llewellyn[3] has pointed out three crucial defects which these indirect methods suffer from: in the first place, these techniques

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1 Gloag on Contract, 399.

2 [1973] 1Q. B.400, 415-416. See also L. Schuler A.G. v. Wickman Machine Tool Sales Ltd. [1974] A.C. 235, 272 where Lord Kilbrandon said: "One must, above all other considerations as I think in a case where the agreement is in obscure terms, see whether an interpretation proposed is likely to lead to unreasonable results, and if it is, be reluctant to accept it".

3 Book Review (1939) 52 Harv. L. Rev. 700, 703.

are all based on the assumption that the clauses and contracts under scrutiny are permissible in content and they thus act as an incentive to draftsmen to improve their workmanship and in future devise more foolproof provisions. Construction, it must be remembered, is in the last instance concerned not with the fairness of contracts but only with the meaning of words as a method of ascertaining the intention of the parties, and no amount of zeal on the part of judges to construe a clause strictly can ultimately change the effect of wholly unambiguous terms.[1] By placing such a high premium on the skill of draftsmen the court merely increases the distress of the party at the receiving end of a standard form, as the offeror of the form contract will usually have greater drafting expertise at his disposal;[2] secondly, by refusing to face the issue squarely, the courts deprive themselves of much needed authority in laying down "minimum decencies" which should be essential prerequisites for enforceability of a contract. It may be added that subsuming the real rationale of relief under construction principles may have the effect that fair and just clauses are also struck down; thirdly, by pretending to construe a contract when they are in fact intentionally misconstruing it, the courts not only increase uncertainty, but also present inadequate remedies. As unfairness is never indicated as the raison d'etre for such "construction" the courts create the impression that these misused techniques are of general application. This generates uncertainty and makes

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1 See Levison v. Patent Steam Carpet Cleaning Co. Ltd. [1977] 3 W.L.R. 90, 95 per Lord Denning M.R.

2 J.H. Baker, The Freedom to Contract without Liability (1971) 24 Curr.Leg. Prob. 53, 66.

the predictability of future judgments very difficult.

Criticism, such as the above, has not been entirely without effect. In the Gillespie Bros. case Lord Denning M.R. maintained that an exemption, limitation or indemnity clause must be construed in the same way as any other clause.

> It should be given its ordinary meaning, that is, the meaning which the parties understood by the clause and must be presumed to have intended. The courts should give effect to the clause according to that meaning - provided always...that it is reasonable as between the parties and is applied reasonably in the circumstances of the particular case.[1]

In that case the Master of the Rolls held that an indemnity clause was "agreed upon, and is reasonable" and should thus be given effect to.

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[1] [1973] 1 Q.B. 400, 416.

3 - FUNDAMENTAL BREACH

Judicial reluctance to allow a party to rely on a clause exempting him from liability where he had committed a serious breach of contract, has been manifested mainly through the practice of construing such a clause narrowly so as not to cover the breach which had occurred. However, the reliance on exemption clauses in such circumstances came to be regarded as so inequitable that for a time the courts recognised a substantive doctrine of fundamental breach. This meant that a particularly serious breach was regarded as tantamount to a repudiation which the innocent party could accept and by doing so, put an end to the entire contract (including the exemption clause), except for the purpose of claiming damages.[1]

Antecedents of the substantive doctrine

The main source of the substantive doctrine of fundamental breach was certain rules of construction developed primarily in cases relating to bailment.

(i) The "deviation" cases: As a result of the fact that the owner of goods may lose the protection of an insurance policy when a sea carrier departs from the agreed route, the courts have held the carrier liable if he so deviates.[2] This naturally led to carriers attempting to exempt themselves from the liability so incurred. In Glynn v. Margetson and Co.,[3] a ship that was under contract to convey

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1 Treitel, Law of Contract, 160.

2 Joseph Thorley Ltd. v. Orchis S.S. Co. [1907] 1K.B. 660.

3 [1893] A.C. 351. See also Sze Hai Tong Bank Ltd. v. Rambler Cycle Co. Ltd. [1959] A.C. 576; Hain Steamship Co. Ltd. v. Tate & Lyle Ltd. [1936] 2 All E.R. 597.

oranges from Malaga to Liverpool first went eastwards and then retraced her course back to Liverpool, with the result that the cargo was found to be damaged on arrival. Despite a printed exemption clause which purported to cover the deviation, the House of Lords were of the opinion that by not proceeding to Liverpool directly, the shipowners had acted inconsistently with the main object and intent of the contract and could therefore not rely on the deviation clause.[1]

(ii) "The four corners rule": It was also established early on that an exemption clause would only protect a party from liability if the contract was performed in the way envisaged by the parties. In Gibaud v. Great Eastern Railway Co. Ltd., Scrutton L.J. expressed the principle as follows:

> /I/f you undertake to do a thing in a certain way, or to keep a thing in a certain place, with certain conditions protecting it, and have broken the contract by not doing the thing contracted for, or not keeping the article in the place in which you have contracted to keep it, you cannot rely on the conditions which were only intended to protect you if you carried out the contract in the way in which you had contracted to do it.[2]

A similar principle has been relied on to render ineffective an exemption clause where, in a contract of sale of goods or hire-purchase, a party performs something essentially different from that contracted for. It has been said that this will occur where, for example, a party promises to deliver peas, but in fact delivers beans[3]

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1 /1893/ A.C. 351, 355 per Lord Herschell, and at 357 per Lord Halsbury.

2 /1921/ 2 K.B. 426, 435. See also The Cap Palos /1921/ P. 458. where the principle expressed by Scrutton L.J. was made applicable to all contracts.

3 Chanter v. Hopkins (1838) 4 M. & W. 399, 404 per Lord Abinger.

or chalk when he promised to provide cheese.[1] In Smeaton Hanscomb & Co. Ltd. v. Sassoon I. Setty, Son & Co., Devlin J. explained that it was

> ... a principle of construction that exceptions are to be construed as not being applicable for the protection of those for whose benefit they are inserted if the beneficiary has committed a breach of a fundamental term of the contract.[2]

A fundamental term, his Lordship maintained, was

> ... something which underlies the whole contract so that, if it is not complied with, the performance becomes something totally different from that which the contract contemplates.[3]

The substantive doctrine

Although Devlin J. in Smeaton Hanscomb still felt compelled to cloak the doctrine in the language of construction it is indicative of the increasing animosity towards unjust exemption clauses that three years later Denning L.J. (as he then was) could say unequivocally that

> /T/hese exempting clauses are nowadays all held to be subject to the overriding proviso that they only avail to exempt a party when he is carrying out his contract, not when he is deviating from it or is guilty of a breach which goes to the root of it.[4]

Similar statements were made in Karsales (Harrow) Ltd. v. Wallis[5] where the parties had contracted for the hire-purchase of a used car.

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1 U.G.S. Finance Ltd. v. National Mortgage Bank of Greece and National Bank of Greece /1964/ 1 Ll. Rep. 446, 453 per Pearson L.J.

2 /1953/ 1 W.L.R. 1468, 1470.

3 Ibid.

4 J. Spurling Ltd. v. Bradshaw /1956/ 1 W.L.R. 461, 465.

5 /1956/ 1 W.L.R. 936.

The car which was eventually delivered to the purchaser, turned out to be substantially different from the one which he had earlier inspected: although it was the same car it had to be towed there, old tyres had been substituted and various parts were missing. Despite the fact that the purchaser refused to accept the car and that it was towed away again, the seller, relying on a clause which provided that no warranty or condition as to the quality of the car was given, claimed ten months' instalments. Denning L.J., in giving judgment for the purchaser, declared:

> /T/he law about exempting clauses has been much developed in recent years, at any rate about printed exempting clauses, which so often pass unread. Notwithstanding earlier cases which might suggest the contrary, it is now settled that exempting clauses of this kind, no matter how widely they are expressed, only avail the party when he is carrying out his contract in its essential respects. ... They do not avail him when he is guilty of a breach which goes to the root of the contract. The thing to do is to look at the contract apart from the exempting clauses and see what are the terms, express or implied, which impose an obligation on the party. If he has been guilty of a breach of those obligations in a respect which goes to the very root of the contract, he cannot rely on the exempting clauses.[1]

The substantive doctrine of fundamental breach soon became a very popular instrument through which the unfair effect of exemption clauses could be prevented. Yeoman Credit, Ltd. v. Apps,[2] for example, again concerned the hire-purchase of a defective used car. The court maintained that there was in the car

> ... an accumulation of defects which, taken singly, might well have been within the exemption clause, but taken en masse constitute such a non-performance or repudiation or breach

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1 Ibid., 940.

2 /1962/ 2 Q.B. 508.

> going to the root of the contract as disentitles the owners to take refuge behind an exception clause intended only to give protection to those breaches which are not inconsistent with and not destructive of the whole essence of the contract.[1]

And in Sze Hai Tong Bank Ltd., v. Rambler Cycle Co. Ltd.[2] where goods had been misdelivered by a carrier, Lord Denning declared that even if the exemption clause were to apply to the breach, it would not protect the carrier as that would defeat one of the "main objects" of the contract.

Suisse Atlantique Societe d'Armement Maritime S.A. v. Rotterdamsche Kolen Centrale[3]

A few judges continued to assert that fundamental breach was not an independent rule of law which was to be applied in disregard of the parties' intentions.[4] This view was vindicated by the House of Lords in the Suisse Atlantique case. Their Lordships unanimously held that the question whether a party could rely on an exemption clause where he had comitted a fundamental breach or where he had breached a fundamental term, was purely a matter of construction of the contract.[5] Lord Wilberforce[6] explained earlier cases (including those proclaiming a substantive doctrine) as instances where, on a proper ascertainment of the intention of the parties, a breach fell outside the scope of an exemption clause.

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1 Ibid., 520. See also Pollock & Co. v. Macrae 1922 S.C. (H.L.) 192.

2 [1959] A.C. 576. Charterhouse Credit Co. v. Tolly [1963] 2 Q.B. 683.

3 [1967] 1 A.C. 361.

4 See, for example, U.G.S. Finance Ltd. v. National Mortgage Bank of Greece and National Bank of Greece [1964] 1Ll.Rep. 446, 450 per Pearson L.J.

5 [1967] 1 A.C. 361, 393, 406, 413, 427, 434; also Photo Production Ltd. v. Securicor Transport Ltd., The Times, 20th February 1980.

6 [1967] 1 A.C. 361, 430 et seq.

According to the opinions expressed by the House of Lords fundamental breach was, therefore, merely an application of the principle that, unless very clear words are used, exemption clauses should not be construed so as to cover a breach which would have the effect of defeating the main purpose of the contract.[1] And even where a clause is so worded that it covers a fundamental breach it might not be given that effect if it "would lead to an absurdity, or because it would defeat the main object of the contract or perhaps for other reasons."[2] Lord Wilberforce also reiterated that

> ... the parties cannot, in a contract, have contemplated that the clause should have so wide an ambit as in effect to deprive one party's stipulations of all contractual force: to do so would be to reduce the contract to a mere declaration of intent.[3]

Fundamental Breach after Suisse Atlantique

The principles underlying fundamental breach were frequently applied long before it acquired the force of a substantive doctrine and since its relegation to a rule of construction it has been similarly used to deprive exemption clauses of effect where they are not expressed clearly enough to cover the breaches that have been committed.[4] Construction, as has been pointed out before, is in any

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1 Treitel, op. cit., 167.

2 [1967] 1 A.C. 361, 398.

3 Ibid., 432.

4 Farnworth Finance Facilities Ltd. v. Attryde [1970] 2 All E.R. 774; Anglo-Continental Holidays Ltd. v. Typaldos Lines [1967] 2 Ll.Rep.61; Levison v. Patent Steam Carpet Cleaning Co.Ltd. [1977] 3 W.L.R.90; Mendelssohn v. Normand Ltd. [1970] 1 Q.B. 177; Wathes (Western) Ltd. v. Austin (Menswear) Ltd. [1976] 1 Ll.Rep.14.

event itself a policy oriented activity[1] so that the limitation imposed by the opinions expressed in the Suisse Atlantique case has not been so restrictive as might have been thought.[2] Exemption clauses which are framed in general terms will be unlikely to free a party from liability for a fundamental breach.[3]

There were indications in some of the speeches in the Suisse Atlantique case that if the innocent party had terminated the contract, as he was justified in doing, the exemption clause would have been ineffectual.[4] These statements were seized on by Lord Denning M.R. in Harbutt's "Plasticine" Ltd. v. Wayne Tank and Pump Co. Ltd.[5] and interpreted in a manner which went a considerable way towards resurrecting fundamental breach as a substantive doctrine. The Master of the Rolls held that where a contract was affirmed by the injured party after the breach, the question whether he could claim damages depended upon a proper construction of the exemption clause, but where the contract was terminated, either by the injured party himself or automatically[6] (because any further performance had become impossible) such a party was entitled to claim damages without the party in breach being entitled to rely on the exemption clause.

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1 Ante,

2 See Treitel, op. cit., 168-169.

3 Ibid. See, for example, Levison v. Patent Steam Carpet Cleaning Co. Ltd. [1977] 3 W.L.R.90 - "at owner's risk".

4 [1967] 1 A.C. 361, 419.

5 [1970] 1 Q.B. 447.

6 See also Photo Production Ltd. v. Securicor Transport Ltd. [1978] 1 W.L.R. 856. The reasoning of the Court of Appeal in that case has been criticised and the decision overturned by the House of Lords in Photo Production Ltd. v. Securicor Transport Ltd., The Times, 20th February, 1980.

Lord Denning's continued espousal of fundamental breach as a substantive doctrine was affirmed by his statement in Levison v. Patent Steam Carpet Cleaning Co. Ltd.[1] that where a party used his superior bargaining power to impose an exemption clause upon the weaker he would not be allowed to rely on it if he himself were guilty of a breach going to the root of the contract.[2]

However, the situation anticipated by Lord Denning will now be dealt with under the provisions of the Unfair Contract Terms Act 1977.[3] That Act has largely obviated the need to resort to fundamental breach in order to cut down the effect of unfair exemption clauses. Nevertheless, where that Act does not apply the principle of fundamental breach will still be of considerable importance.

Policy considerations underlying fundamental breach

Professor Coote expressed the real rationale behind the doctrine of fundamental breach when he said that

> ... the opprobrium which attaches to extravagant exception clauses, and the general reaction against laissez-faire notions of the nineteenth century, together assured that the new concepts of fundamental breach and fundamental term would receive an enthusiastic welcome, both from the courts and from academic writers. Here at last, it seemed, was a way in which justice might be served and the monopolists contained.[4]

Time and time again the courts focussed on the unreasonableness of allowing a party who committed a fundamental breach to exclude

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1 /1977/ 3 W.L.R. 90.

2 Ibid., 97.

3 Post, 320. See especially sections 9 and 22.

4 Exception Clauses, 108.

liability by relying on an exemption clause.[1] And in Levison v. Patent Steam Carpet Cleaning Co. Ltd. Lord Denning admitted that "/t/he ... means of getting round the injustice of these exception or limitation clauses is by means of the doctrine of fundamental breach."[2] And the reason why these clauses are unjust, Lord Denning said, is because of the illusion created by promising to do something, but at the same time adding that you are not to be held liable if you do not perform accordingly.[3]

The courts clearly disapproved of the fact that a promisor could, by invoking the exemption clause, substantially alter the value of the promisee's bargain and the quantum of remedies available to and against him, and thereby frustrate the promisee's legitimate expectations. The operation of the doctrine was not dependent upon any showing of procedural unfairness or that the exemption clause was commercially unjustified. It was rather a direct attempt to impose certain "minimum decencies" on contract. It presupposed that every contract had a number of core duties which could not be detracted from. The basis of this transactional essence was the legitimate expectations created by the contract itself. Any term which detracted from the "iron essence" of the contract would, in terms of the doctrine, be ineffective.[4]

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1 See, for example, Sze Hai Tong Bank, Ltd. v. Rambler Cycle Co. Ltd. /1959/ A.C. 576.

2 /1977/ 3 W.L.R. 90, 96.

3 Ibid., 96-97.

4 Cf. Llewellyn, The Common Law Tradition, 362-371.

Criticism of Fundamental Breach

The difficulties involved in a substantive doctrine of fundamental breach related, in the first place, to the real effect of an exemption clause. Contrary to conventional wisdom which maintained that in order to establish the content of a party's obligations one should look to the contract apart from the exempting clauses,[1] Coote asserted that there are two classes of exemption clauses:

> Type A: exception clauses whose effect, if any, is upon the accrual of particular primary rights.... Type B: exception clauses which qualify primary or secondary rights without preventing the accrual of any particular primary right.[2]

The distinction between these types of exemption clauses was important because "/i/nstead of being mere shields to claims based on breach of accrued rights /Type A/ exception clauses substantively delimit the rights themselves"[3] with the result that what might ordinarily have amounted to a fundamental breach was prevented from becoming so as a result of the operation of the exemption clause. Courts have been reluctant to accept this formula,[4] presumably because they realized that it would severely limit their power of "getting at" unfair exemption clauses.

Secondly, the inability of accurately circumscribing the "core of the contract", or the "fundamental term" made it difficult to develop the doctrine rationally with the result that its application was of necessity inconsistent. Thirdly, the doctrine of fundamental breach

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1 See, for example, Karsales (Harrow) Ltd. v. Wallis /1956/ 1 W.L.R. 936, 940 per Lord Denning M.R.

2 Exception Clauses, 9.

3 Op. cit., 17.

4 See, however, Kenyon, Son & Craven Ltd. v. Baxter Hoare & Co.Ltd., /1971/ 1 W.L.R. 519, 522 per Donaldson J.

because it operated only where a breach had been serious, presented no solution to the broader problem of unfair terms in standardized contracts: where a breach had only been minor the exemption clause would still operate no matter how widely worded it was.

A Substantive doctrine of fundamental breach in Scots law?[1]

It was established in Wade v. Waldon[2] that a party may rescind a contract only when there has been a material breach or a breach which goes to the root of the contract. Lord President Dunedin explained the meaning of such a breach as follows:

> It is familiar law, and quite well settled by decision, that in any contract which contains multifarious stipulations there are some which go so to the root of the contract that a breach of those stipulations entitles the party pleading the breach to declare that the contract is at an end. There are others which do not go to the root of the contract, but which are part of the contract, and which would give rise, if broken, to an action of damages.[3]

Whether a term is material or not will depend upon construction. It has been said that if the failure to perform a contractual obligation "would make the performance of the rest of the contract a different thing from what the other party had stipulated for"[4] the innocent party is entitled to rescind.

Some Scottish cases have been reluctant to allow exemption clauses to undercut an innocent party's remedies where the breach has

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1 See generally, J.M. Thomson, Fundamental Breach in Scots and English Law,(1977) 22 Jur.Rev. 38, 47-55.

2 1909 S.C. 571.

3 Ibid., 576.

4 Gloag on Contract, 602, cited with apparent approbation in Alexander Stephen (Forth) Ltd. v. J.J. Riley (U.K.) Ltd. 1976 S.L.T. 269. See also Thomson, op. cit., 49.

been material. In Hamilton v. The Western Bank of Scotland,[1] the Lord Ordinary (Lord Jerviswoode) declared that

> where there is a flaw which strikes at the contract itself, and which would suffice to annul it, nothing short of a positive declaration that the purchaser shall be held to have no remedy in such a case can bar his right to restoration against it.[2]

It has even been hinted at by Lord President Cooper while discussing the validity of exempting conditions contained in an airline ticket, that excessively wide exemption clauses might not be legal:

> The remarkable feature of these conditions is their amazing width, and the effort which has evidently been made to create a leonine bargain under which the aeroplane passenger takes all the risks and the company accept no obligations, not even to carry the passenger or his luggage nor even to admit him to the aeroplane. It was not argued that the conditions were contrary to public policy, nor that they were so extreme as to deprive the contract of all meaning and effect as a contract of carriage; and I reserve my opinion upon these questions.[3]

Scots law has not, however, gone so far as to accept the substantive doctrine of fundamental breach. In the first case in which the doctrine was expressly discussed, Alexander Stephen (Forth) Ltd. v. J.J. Riley (U.K.) Ltd.,[4] the Lord Ordinary (Kincraig) described fundamental breach in Scots law as "the breach of a material condition of the contract which justifies the other party in rescinding it."[5] Lord Kincraig furthermore accepted the opinion of the House of Lords

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1 (1861) 23D. 1033.

2 Ibid., 1037. See also Stevenson v. Henderson (1873) 1R. 215.

3 McKay v. Scottish Airways 1948 S.C. 254, 263. See also the similar hint by Lord Cowan in Stevenson v. Henderson (1873) 1R. 215, 223.

4 1976 S.L.T. 269.

5 Ibid., 272.

in Suisse Atlantique that the question whether an exemption clause covered such a breach depended on a proper construction of the contract and he held that the clause in the Stephen case was in sufficiently clear language for it to be relied on by the party in breach notwithstanding the fact that the injured party had rescinded the contract.[1]

In the subsequent case of W.L. Tinney & Co. Ltd. v. John C. Dougall Ltd.[2] Lord Wylie said that a limitation or exclusion clause had to be spelt out in the clearest possible terms in order to be effective in the event of a breach. He accepted the statement by Lord Wilberforce in Suisse Atlantique[3] that the more radical the breach the clearer the language had to be if it was to be covered and, construing the clause contra proferentem, held that the defenders could not in the circumstances rely on it.

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1 Ibid.

2 1977 S.L.T. (Notes) 58.

3 [1967] 1 A.C. 361, 432.

4 - IMPLIED TERMS[1]

The courts, when construing a contract, often impose terms in order to reform an otherwise unfair agreement. During the nineteenth century the prevailing jurisprudence dictated that all implied terms should be relayed back to the parties' intentions. It was accordingly said that terms would be implied only if they were necessary to give a contract business efficacy in a manner intended by the parties,[2] or to make the agreement workable in a manner in which the parties would have done had they applied their minds to it. In Shirlaw v. Southern Foundries (1926) Ltd.,[3] Mackinnon L.J. expressed the test as follows:

> Prima facie that which in any contract is left to be implied and need not be expressed is something so obvious that it goes without saying; so that, if, while the parties were making their bargain, an officious bystander were to suggest some express provision for it in their agreement, they would testily suppress him with a common, 'Oh, of course!'[4]

As a result of the need to relate every implied term to the intention of the parties, this technique of implication, known as implication in fact, occurs comparatively rarely.[5] A term will, for example, not be implied where one of the parties was unaware of the facts on which the implied term is to be based.[6] Similarly, a term will not be implied if it cannot be defined with a high degree

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1 See, generally, E.A. Farnsworth, Disputes over Omission in Contracts (1968) 68 Col.L.Rev.860.

2 Luxor (Eastbourne) Ltd. v. Cooper [1941] A.C. 108, 137; Shell U.K. Ltd. v. Lostock Garages Ltd. [1976] 1 W.L.R.1187, 1197.

3 [1939] 2 K.B. 206.

4 Ibid., 227; Young and Marten Ltd. v. McManus Childs Ltd. [1968] 2 All E. R. 1169, 1172.

5 Treitel, Law of Contract, 145.

6 McCutcheon v. David MacBrayne Ltd. [1964] 1 W.L.R. 125.

of precision by the courts,[1] for in such a case it is impossible to impute the term to the intention or presumed intention of the parties.

However, determining what the parties intended depends primarily on the construction of the contract and in doing so the court will to some extent, be influenced by its own view of what the parties ought to have intended.[2] Although the "obviousness" and "necessity for business efficacy" tests are not wide enough to allow implication of a term in every case where it would be reasonable to do so, they are sufficiently flexible yardsticks for the court at least to take into account all the circumstances of the case and to balance the interests of the parties in the process of deciding whether a term should be implied or not.[3]

However, the mere fact that a term cannot be implied in fact does not mean that implication is impossible. The courts also imply a variety of terms which cannot be defined by or ascribed to the intention of the parties.[4] These consist mainly of duties which the courts impose in particular types of contract - a vendor of a business must not entice away the purchaser's customers,[5] a landlord covenants that the tenant shall have quiet possession, a depositary in a contract of locatio conductio operis must exercise reasonable

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1 Cf. Shell U.K. Ltd. v. Lostock Garages Ltd. /1976/ 1 W.L.R. 1187, 1204 per Bridge L.J.

2 J.F. Burrows, Contractual Co-operation and the Implied Term (1968) 31 Mod.L.Rev. 390, 406. See also Gloag on Contract, 289 who maintains that the test is whether two reasonable men would have included the term. Also Morton v. Muir Bros. 1907 S.C.1211, 1224.

3 Burrows, op.cit.

4 G. Williams, Language and the Law (1945) 61 L.Q.R. 401.

5 Trego v. Hunt /1896/ A.C.7.

care[1], a builder of a house guarantees that it will be reasonably fit for human habitation.[2] In these cases neither the existence nor the extent of the duty can be determined by reference to the intention or even the presumed intention of the parties. It is, therefore, clear that when the courts impose such obligations on the parties they are concerned with the intention of the parties only in so far as a clear contrary intention would serve to exclude such an implication.[3]

What then is the basis upon which such terms are implied? It has been suggested that policy considerations[4] underlie the imposition by the courts of these duties. According to Gloag

> /I/n the earlier history of the law of Scotland the Court seems generally to have proceeded on equitable grounds rather than on any evidence of general practice in similar or analogous cases. Thus where a lease contained no provision as to the term of entry, the implication that an immediate term of entry was to be inferred, now regarded as an integral part of the law of landlord or tenant seems originally to have been arrived at simply on the ground that to the judicial mind it appeared fair and reasonable without any evidence as to practice in other cases.[5]

It would appear as if Scots contract law, like the civilian jurisdictions, has been more prepared to impose general obligations in particular types of contract without the necessity of imputing it to the parties' intentions. In earlier times this was usually done by virtue of the requirement of bona fides.[6]

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1 Forbes v. Aberdeen Motors Ltd. 1965, S.L.T. 333, 337.

2 Hancock v. B.W. Brazier (Anerley) Ltd. /1966/ 1 W.L.R. 1317, 1330.

3 Williams, op. cit.

4 Treitel, op. cit., 148.

5 Op. cit., 289-290.

6 Ante, 179 et seq.

The realization that contractual duties are frequently implied in order to do justice between the parties has similarly led Lord Denning M.R. to espouse the view that they are implied whenever it is reasonable to do so.[1] In Liverpool City Council v. Irwin[2] the Council built a towerblock and let the flats out to tenants. In terms of the tenancy agreements the Council retained control of the lifts and staircases. The agreements imposed certain obligations on the tenants but none in respect of the Council. The parts of the building over which the Council had control deteriorated badly and the question before the court was whether there was an implied obligation on the Council to keep them in repair. Roskill and Ormrod L.JJ. held that because implication of a term was not necessary for the business efficacy of the contract no such obligation could be implied.[3] Lord Denning, on the other hand, thought that such an obligation could be implied, but that it had not been breached. He based his argument for the implication of such a term on the fact that such a term would be reasonable in the circumstances.

> It is often said that the courts only imply a term in a contract when it is reasonable and necessary to do so in order to give business efficacy to the transaction... (Emphasis is put on the word "necessary" ...). Or when it is obvious that both parties must have intended it ...
>
> Those expressions have been repeated so often that it is with some trepidation that I venture to question them. I do so because they do not truly represent the way in which the courts act. Let me take some instances... Such as the terms

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1 Greaves & Co. (Contractors) Ltd. v. Baynham Meikle & Partners [1975] 1 W.L.R.1095, 1099-1100; Federal Commerce and Navigation Co.Ltd. v. Tradax Export S.A. [1977] 2 W.L.R.122, 133. Contra Reigate v. Union Manufacturing Co.(Ramsbottom) Ltd. [1918] 1 K.B. 592,605.

2 [1976] Q.B.319.

3 Ibid., 337-338, 343.

> implied by the courts into a contract for the sale of goods... into a contract for work and materials ... or into a contract for letting an unfurnished house... or a furnished house... or into the carriage of a passenger by railway ... or to enter on premises... or to buy a house in course of erection...
>
> If you read the discussion in those cases, you will see that in none of them did the court ask: what did both parties intend? If asked, each party would have said he never gave it a thought: or the one would have intended something different from the other. Nor did the court ask: Is it necessary to give business efficacy to the transaction? If asked, the answer would have been: "It is reasonable, but it is not necessary." The judgments in all those cases show that the courts implied a term according to whether or not it was reasonable in all the circumstances to do so. Very often it was conceded that there was some implied term. The only question was: "What was the extent of it?" Such as, was it an absolute warranty of fitness, or only a promise to use reasonable care? That cannot be solved by inquiring what they both intended, or into what was necessary. But only into what was reasonable. This is to be decided as matter of law, not as matter of fact.[1]

Although on appeal [2] the House of Lords affirmed Lord Denning's finding that the Council was under an implied obligation to repair the common parts, their Lordships did not approve of his reasoning. The House was of the opinion that a distinction should be drawn between a search for a term which might be necessary for business efficacy and the implication of "such a term as the nature of the contract might call for or as a legal incident of this kind of contract."[3] In respect of this latter category - which comprises all contracts of common occurrence - the court, when deciding whether or not to imply a term, does not look to the intention or presumed intention of the

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1 Ibid., 329-330.

2 [1967] 2 W.L.R. 562.

3 Ibid., 568 per Lord Wilberforce.

parties. It should in the first place, determine whether an obligation has already become established as a rule of law in similar types of contract, and if so, it should impose such a duty in all similar factual settings.[1] If, on the other hand, the courts have not yet defined the obligation they may still do so on the basis of "wider considerations"[2] According to Lord Cross

> /W/hen it implies a term in a contract the court is sometimes laying down a general rule that in all contracts of a certain type - sale of goods, master and servant, landlord and tenant and so on - some provision is to be implied unless the parties have expressly excluded it. In deciding whether or not to lay down such a prima facie rule the court will naturally ask itself whether in the general run of such cases the term in question would be one which it would be reasonable to insert.[3]

The House of Lords felt that the contract between the Council and the tenant fell within this category. So Lord Wilberforce held that "/T/he subject-matter of the lease (high rise blocks) and the relationship created by the tenancy demands, of its nature, some contractual obligation on the landlord."[4] To hold otherwise would be contrary to "common sense"[5] and would render the whole transaction "inefficacious, futile and absurd."[6] The extent of the obligation which the court imposes must be such as is reasonable in the circumstances.[7]

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1 See Shell U.K. Ltd. v. Lostock Garages Ltd. /1976/ 1 W.L.R.1187, 1196 per Lord Denning M.R.

2 /1976/ 2 W.L.R. 562, 568.

3 Ibid., 570.

4 Ibid., 567.

5 Ibid., 572 per Lord Cross.

6 Ibid., 574 per Lord Salmon.

7 Ibid., 569 per Lord Wilberforce.

The House of Lords clearly regarded Lord Denning's proposal that terms should be implied when it is reasonable to do so as too wide. Reasonableness may, however, be one of the "wider considerations" which the court takes into account when deciding whether or not to impose a duty on a party. The House of Lords was undoubtedly correct in maintaining that the courts do not impose terms merely because doing so would render a harsh contract more fair. That does not, however, mean that a court will imply a term the effect of which is unreasonable in the circumstances.[1] The main objection to laying down a rule like that proposed by Lord Denning rests on freedom of contract. It is clearly felt that to imply terms on the sole ground of a standard as undefined as reasonableness would provide too great a threat to the sanctity of contracts. However, such an objection relates only to the outer limits of implication and not to its effect, which is often to do justice between the parties. This is shown by the Liverpool City case where the House of Lords, contrary to the general rule that the owner of an easement is not responsible for maintenance of the property, imposed on the Council an obligation to repair because that was "just".[2] If, as the House of Lords maintains, a duty may be imposed on a party by virtue of the fact that the nature of the contract requires it and the effect of such an implication is to do justice between the parties, the question arises why the courts may not base their implication directly on reasonableness. There is no

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1 Ibid., 580 per Lord Edmund-Davies. See also Young and Marten Ltd. v. McManus Childs Ltd. /1969/ A.C. 454, 465 per Lord Reid.

2 Ibid., 570 per Lord Wilberforce.

reason to believe that where a contract is of a kind where the rights and duties have not yet been clearly defined by precedent the "nature of the contract" is a less uncertain standard than a standard of reasonableness. In addition, although a standard such as that proposed by the House of Lords may be sufficient to indicate that a duty must be imposed on one of the parties in order to make the contract effective it cannot by itself allocate the party who is to bear the duty. Whether the one or the other party is to undertake an obligation can only be arrived at by balancing the interests of the respective parties and by determining what would be reasonable in the light of all the circumstances of the case.

5 - A COMMON LAW REQUIREMENT OF REASONABLENESS

(i) Contracts in restraint of trade

One of the few areas in Scots and English law in which the application of a reasonableness test has become institutionalised is that related to contracts in restraint of trade. In this field two fundamental principles, namely freedom of contract and freedom of trade, conflict.

There are very few reported cases on the subject in early Scots law[1], but it would seem as if restrictive covenants in contracts were enforced unless they were particularly restrictive of personal liberty.[2] However, since the end of the nineteenth century Scots law has generally followed an approach similar to English law.[3]

In English law contracts in restraint of trade were originally void, but after the subject was re-examined in Mitchel v. Reynolds,[4] they were generally treated as prima facie valid, provided the restraint was limited and supported by adequate consideration. This approach continued into the nineteenth century, but the requirement of adequate consideration became progressively less important and was eventually not insisted on.[5] In Nordenfelt v. Maxim Nordenfelt Guns & Ammunition Co.[6] the doctrine was again reviewed and restated in its modern form.

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1 McBryde, Void, Voidable, Illegal and Unenforceable Contracts in Scots Law, 148-149.

2 Stalker v. Carmichael 1735 Mor. 9455.

3 See, for example, Mulvein v. Murray 1908 S.C. 528; MacIntyre v. Cleveland Petroleum Co.Ltd. 1967 S.L.T. 95.

4 (1711) 1 P.Wms. 181.

5 Hitchcock v. Coker (1837) 6 Ad. & El. 438.

6 [1894] A.C. 535.

Since then contracts in restraint of trade are prima facie void, unless it can be shown that the restraint is reasonable inter partes and not contrary to public interest. In general, a restraint will be upheld only if it goes no further than is reasonably necessary for the protection of the covenantee's legitimate interests.

The doctrine did not remain unaffected by the principle of freedom of contract. Although the courts were prepared to intervene in the traditional areas such as restraints imposed by employers to prevent former employees from competing with them and those imposed by buyers of businesses to protect their goodwill against the competition of the seller, they were far more reluctant, especially towards the end of the nineteenth century and during the first half of the twentieth century, to invalidate price fixings and business arrangements which resulted in monopolies and prevented competition.[1] According to Atiyah[2] this attitude was the result of the courts' obsession with freedom of contract: it was assumed that if commercial parties had freely agreed to a restriction it was reasonable between them and if that was the case it would be presumed not to be contrary to the public interest. The result was that freedom of trade became subordinated to freedom of contract.

Recently, however, the scope of the doctrine has been considerably extended to include some exclusive dealing and services arrangements.[3] In Esso Petroleum Co. Ltd. v. Harper's Garage (Stourport)

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1 Atiyah, The Rise and Fall of Freedom of Contract, 697-703.

2 Op. cit., 699.

3 See generally J.D. Heydon, Recent Developments in Restraint of Trade (1975) 21 McG.L.J. 325.

Ltd.[1] the House of Lords set aside, on the ground that it was restrictive of trade, a so-called solus agreement between a petrol company and a garage owner, whereby the latter had bound himself for twenty-one years to buy petrol from the former at their scheduled prices. The Esso case provided a clear indication that the courts were henceforth going to be much more vigilant against practices which prevent competition and free trade. However, complete freedom of trade as an ideal is neither attainable nor always desirable. For example, the exclusive dealing arrangements have considerable benefits not only for the parties involved, but also as regards the public at large. The question therefore, is not whether to allow or to strike down all restrictive covenants, but how to demarcate the frontiers beyond which a restraint will not be tolerated.

In Esso Lord Pearce suggested that the doctrine applies where the restraint sterilizes trade and not where it merely regulates the "normal commercial relations between the parties."[2] And in a later case Lord Reid said that "if contractual restrictions appear to be unnecessary or to be reasonably capable of enforcement in an oppressive manner, then they must be justified before they can be enforced."[3] In Instone v. A. Schroeder Music Publishing Co., Ltd.,[4] a case in which an agreement whereby songwriters undertook to give their exclusive services to a firm of music publishers, was held to be unenforceable,

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1 /1968/ A.C. 269. See also Amoco Australia Ply Ltd. v. Rocca Bros. Motor Engineering Ply Ltd. (1973) 47 A.L.J.R.681.

2 Ibid., 327.

3 A. Shroeder Music Publishing Co.Ltd. v. Macaulay /1974/ 1 W.L.R. 1308, 1314., formerly Instone v. A. Schroeder Music Publishing Co.Ltd. /1974/ 1 All E.R. 171.

4 /1974/ 1 All E.R. 171.

Russell L.J. rightly rejected this method of classification as pre-empting the question of reasonableness, and said:

> Rather than attempt to classify some situations involving restrictions on trade as 'restraints of trade' and other situations as not, we would prefer a quite general approach to all such situations.[1]

In the Esso case the House of Lords declared the contract unenforceable primarily on the ground that it was contrary to the public interest and in doing so stressed the importance of considering the effect of such agreements on freedom of trade. This must not, however, be taken to mean that the court should embark on an equiry into the effect of a restriction on the general social and economic conditions. In Texaco Ltd. v. Mulberry Filling Station Ltd.,[2] Ungoed-Thomas J. rightly warned that the court is not equipped to deal with an inquiry of that nature and scope. To regard freedom of trade as anything other than a general statement of policy will involve the court in every restraint of trade case in an inquiry, the proportion of which will correspond to those undertaken in anti-trust cases in the U.S.A.

Esso was not decided solely on the basis of public interest. Lord Reid also expressed the opinion that a party who agrees to a restriction should receive some compensating advantage and that in that respect, the quantum of consideration was of considerable importance.[3] In A. Schroeder Music Publishing Co.Ltd. v. Macaulay[4]

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1 Ibid., 177. For another application of the doctrine to a similar factual setting see Clifford Davis Management Ltd. v. W.E.A. Records Ltd. [1975] 1 W.L.R. 61.

2 [1972] 1 W.L.R. 814, 827.

3 [1968] A.C. 269, 300.

4 [1974] 1 W.L.R. 1308.

the House of Lords similarly based their opinion that the contract should not be enforced, almost entirely on the unreasonableness of the restriction inter partes. Lord Diplock said:

> It is, in my view, salutary to acknowledge that in refusing to enforce provisions of a contract whereby one party agrees for the benefit of the other party to exploit or to refrain from exploiting his own earning power, the public policy which the court is implementing is not some 19th-century economic theory about the benefit to the general public of freedom of trade, but the protection of those whose bargaining power is weak against being forced by those whose bargaining power is stronger to enter into bargains that are unconscionable.[1]

Just as in Esso, the House emphasized the fact that while the songwriter was bound to give his services exclusively to the publishing company, they undertook no obligations in return.[2] And in Clifford Davis Management Ltd. v. W.E.A. Records Ltd.,[3] Lord Denning M.R. similarly refused enforcement of an agreement, potentially effective for ten years, whereby a songwriter bound himself to turn over all his compositions to a publisher, who undertook no obligation to publish them, and referred to the arrangement as a "stranglehold".[4]

In the Esso case Lord Reid suggested that even where it has been established that an agreement is unfairly restrictive the court might not intervene if the parties were two experienced traders bargaining on equal terms.

> But there may well be cases where, although the party to be restrained has deliberately accepted the main terms of the contract, he has been at a disadvantage as regards other

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1 Ibid., 1315.

2 Ibid., 1313 per Lord Reid.

3 [1975] 1 W.L.R.

4 Ibid., 63.

> terms: for example where a set of conditions has been incorporated which has not been the subject of negotiation - there the court may have greater freedom to hold them unreasonable.[1]

In the Schroeder case Lord Diplock, in holding the contract unreasonable in terms of the restraint of trade doctrine, similarly emphasized the fact that the agreement between the songwriter and the publisher was in standard form. He distinguished two types of standard form contract. Firstly, there are those such as bills of lading and charterparties in which the standard clauses have been settled over the years by negotiation and have been adopted because they facilitate trade. The fact that they are widely used by parties whose bargaining power is fairly matched make them prima facie reasonable. This presumption does not arise in the case of the second type of standard form contract, which is of relatively recent origin.

> The terms of this kind of standard form of contract have not been the subject of negotiation between the parties to it, or approved by any organisation representing the interests of the weaker party. They have been dictated by that party whose bargaining power, either exercised alone or in conjunction with others providing similar goods or services, enables him to say: 'If you want these goods or services at all, these are the only terms on which they are obtainable. Take it or leave it.'
>
> To be in a position to adopt this attitude towards a party desirous of entering into a contract to obtain goods or services provides a classic instance of superior bargaining power.[2]

The fact, Lord Diplock continued, that a party's bargaining power is strong enough to adopt this take-it-or-leave-it attitude does not raise a presumption that he drove an unconscionable bargain, but

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1 [1968] A.C. 269, 300.

2 [1974] 1 W.L.R. 1308, 1316.

where it results in a restraint on a party it calls for judicial vigilance.

To summarise: According to Russell L.J.[1] all restraints, or, if the view of the House of Lords[2] is accepted, those restraints which are oppressive, must be subjected to the tests of the restraint of trade doctrine. The tests must take the interest of the public in free trade into account, but they should, in the main, focus on the reasonableness of the restraint inter partes. A contract will normally be unreasonable if it is one-sided or stipulates for an unequal exchange or if it unreasonably fetters a party or puts him in a stranglehold. Even so, a court will be reluctant to refuse enforcement if the contract was concluded by experienced parties of equal bargaining power. On the other hand, if one party merely had to accede to another's standard terms it will be an indication of unequal bargaining power and relief will be granted more readily.

Two criticisms can be levelled at this approach. The first deals with the nature of standard form contracts and is thus also relevant outside the sphere of the restraint of trade doctrine. The drift of Lord Diplock's argument in the Schroeder case seems to be that the use of standard form contracts is proof of a concentration of market power and consequently, that a party who uses standard form contracts has bargaining power superior to that of his counterpart.[3]

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1 Instone v. A. Schroeder Music Publishing Co. Ltd. /1974/ 1 All E.R. 171, 177.

2 A. Schroeder Music Publishing Co.Ltd. v. Macaulay /1974/ 1 W.L.R. 1308, 1314.

3 Ibid., 1316.

A similar assumption was made by Lord Denning in Clifford Davis.[1] In a perceptive discussion of the former case Trebilcock[2] has convincingly argued that not only is it not necessarily true that the use of standardized contracts result from market concentration in a few hands, but the fact that there was no negotiation of the terms is not in itself significant in respect of the question of bargaining power and becomes so only if the party has no other means of fulfilling his needs. Superior bargaining power arising from the market structure can only be assumed after an inquiry has shown that no alternative sources of supply were open to the party.[3] Thereafter the court will have to establish that a particular contract or clause in a contract was a product of bargaining imbalance. It should be clear that the use of unequal bargaining power arising from the market structure as a reason for non-enforcement presupposes factual inquiries which the courts are not qualified to embark on.[4] The courts cannot redress inequalities which are basic to the economic system.

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1 /1975/ 1 W.L.R. 61, 65.

2 M.J. Trebilcock, The Doctrine of Inequality of Bargaining Power: Post Benthamite Economics in the House of Lords (1976) 26 U.Toronto L.J. 359, 364-366. Trebilcock rightly points out that not only does the evidence in the Schroeder case indicate that the songwriter had other outlets for his compositions which he rejected because the publisher eventually chosen offered wider markets, but also that some terms of the standard form contract were actually changed after representations by the composer.

3 See, for example, A Schwartz, Seller Unequal Bargaining Power and the Judicial Process (1974) 49 Indiana L.J. 367.

4 Ibid., 384-386.

This does not mean that inequality of bargaining power arising from sources other than market structure cannot be employed as a reason for striking down unfair contracts or that unfairness perpetrated through the use of standard form contracts should be tolerated. It does mean, however, that inequality of bargaining arising from the market structure and supposedly evidenced by the use of standard form contracts cannot be assumed without a wide-ranging inquiry which the court is not qualified to undertake. The courts should not - as they did in the Schroeder and Clifford Davis cases - base on inequality of bargaining power, decisions reached on other grounds. They should instead, in the field of contracts in restraint of trade, do what they have been doing in effect if not in theory, and that is to delimit on policy or moral grounds the points beyond which restraints on parties will not be allowed.

In the Schroeder case Lord Diplock said that the test of fairness involved asking

> whether the restrictions are both reasonably necessary for the protection of the legitimate interests of the promisee and commensurate with the benefits secured to the promisor under the contract.[1]

Lord Reid compared the respective promises and said that although the songwriter had to assign the copyright in all his compositions to the publisher for a five and possibly ten year period, he received little payment (apart from royalties in case of publication) and the publisher was under no obligation to publish his work. In addition, the composer had no right to terminate the agreement or to have the copyright re-

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[1] [1974] 1 W.L.R. 1308, 1315-1316.

assigned to him.[1] In the Clifford Davis case Lord Denning, on substantially similar facts, voiced the same objections.[2]

While admitting that the types of promise contained in these contracts may often be so open-ended as to amount to no legal obligation at all, the question still arises as to what type of obligation one could reasonably expect the publishers to have undertaken in the circumstances. Indeed, in the Schroeder case Lord Reid recognised that it would have been unreasonable to have required from him a definite commitment to publish the songs.[3] It therefore seems somewhat unfair to punish him for something which the court admits could not be done. While recognising that the imbalance in the obligations undertaken is an important consideration in deciding on the reasonableness of a restraint it is suggested that the test should essentially focus on the extent to which a party's liberty is curtailed by the restraint. The question then is not solely whether the restricted party received an adequate consideration, but whether he was caught in a "stranglehold" or became so subjugated to another that his entire economic existence was controlled by that other party. This aspect after all, lies at the heart of the restraint of trade doctrine.[4] It is a test which deals with the terms and the effect of the restraint and not with the imbalance in market power that may have produced it.

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1 Ibid., 1314-1315.

2 [1975] 1 W.L.R. 61, 65.

3 [1974] 1 W.L.R. 1308, 1314.

4 See, for example, Esso Petroleum Co. Ltd. v. Harper's Garage (Stourport) Ltd. [1968] A.C. 269, 323 per Lord Pearce, 332-333 per Lord Wilberforce.

When a restraint is so fettering as to become unreasonable is a difficult question and the courts can only mark out the bounds of the permissible by reference to the commercial context in which the contract was to operate.

(ii) Contracts other than restraint of trade

It has been suggested in a few obiter dicta that a contract term will only be enforced if it is reasonable or if it is reasonable for the party wishing to rely on it to do so. These suggestions were first made in a small number of late nineteenth[1] and early twentieth century[2] ticket cases. In view of the far-fetched example of unreasonableness cited by one of the judges,[3] namely a term whereby the owner of goods deposited at a cloakroom shall forfeit £1,000 if he fails to collect them within forty-eight hours, it is not surprising that there is no indication that the test was ever successfully applied at the time.

More recently, a similar test has been proposed and applied by Lord Denning in a number of cases dealing with standard form contracts. Jaques v. Lloyd D. George and Partners Ltd.[4] concerned the validity of a term as to the time when an estate agent's commission became payable. The term, which was contained in the estate agent's

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1 Van Toll v. The South Eastern Railway Co. (1862) 12 C.B. (N.S.)75, 88; Parker v. The South Eastern Railway Co. (1877) 2 C.P.D. 416, 428.

2 Thompson v. London, Midland and Scottish Railway Co. [1930] 1 K.B. 41, 53.

3 Bramwell L.J. in Parker v. The South Eastern Railway Co. (1877) 2 C.P.D. 416, 428.

4 [1968] 1 W.L.R. 625.

printed terms of business, was inconsistent both with representations made in the pre-contract negotiations and the usual practice in these cases. In holding the clause to be invalid Lord Denning suggested as an alternative ground that the clause was unreasonable. He maintained that if an estate agent wished to depart from the commission clause as usually understood it should be brought home very clearly to the client. In the absence of such an explanation, the client was entitled to assume that there was nothing unreasonable or oppressive in the contract. If the client did not read the contract and if it was afterwards found to contain unreasonable terms, then it should not be enforced.

This view was reiterated in Gillespie Bros. and Co. Ltd. v. Roy Bowles Transport Ltd., Rennie Hogg Ltd.,[1] a case concerning the effectiveness of an indemnity clause. The Master of the Rolls reviewed the traditional judicial techniques of controlling terms which restrict the liability of parties for their own negligence and asserted that in all the instances where the courts have granted relief from them they did so because they regarded the clauses as unreasonable. The courts "will not allow a party to exempt himself from his liability at common law when it would be quite unconscionable for him to do so."[2] However, "/w/hen such a clause is agreed upon, and is reasonable, it should be given effect according to its terms."[3]

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1 /1973/ Q.B. 400.

2 Ibid., 416.

3 Ibid., 417.

The clause was reasonable in that case, said Lord Denning, because it was common practice for carriers to limit their liability to specific amounts and leave the owner of the goods to insure if he wished to have greater cover. In effect, therefore, the clause was reasonable because it was agreed to, and it was agreed to because the party was deemed to have known about the clause, even if, in fact, he was unaware of it.

The most recent case, Levison v. Patent Steam Carpet Cleaning Co. Ltd.,[1] concerned the validity of a limitation clause contained in an order form. The plaintiff had arranged with the defendant company to collect for cleaning a Chinese carpet valued at £900. At the time of collection the plaintiff was requested to sign an order form containing certain conditions and he complied without reading those provisions. The effect of clause 2 was to limit the liability of the defendant in respect of damage to the carpet to £40, and clause 5 provided that goods were "expressly accepted at the owner's risk" and that therefore the owners were recommended to insure their property. The carpet was lost while at the cleaners and the plaintiff claimed damages. The Court of Appeal held that the defendant could not limit its liability by relying on the limitation clause. Lord Denning simply assumed that because the terms under which the cleaning was undertaken were the cleaner's standard terms of business it was an instance of superior bargaining power.[2] He referred to the Gillespie Bros.

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1 [1977] 3 W.L.R. 90.

2 Ibid., 94.

case and said:

> I suggested that an exemption or limitation clause should not be given effect if it was unreasonable, or if it would be unreasonable to apply it in the circumstances of the case. I see no reason why this should not be applied today, at any rate in contracts in standard forms where there is inequality of bargaining power. In this case I would apply it in this way: take the limitation clause ... In some circumstances that clause might be reasonable. But it would not in the present case be reasonable to allow the cleaning company to rely on it. They knew that they were to collect a heavy Chinese carpet which was worth a lot of money. To limit liability to £40 (without a word of warning) would, I think, be most unreasonable.[1]

The same considerations applied, Lord Denning maintained, in relation to clause 5.

The nature of the reasonableness test, as set out by Lord Denning, has been moulded by the factual setting in which it has been applied. The question in every case was whether the party against whom a clause operated was aware of it and understood its purport. If it was not brought to his attention or if it was not a case where he ought to have been aware of the clause then it would be unreasonable for the proferens to rely on it. The clauses were, in effect therefore, struck down not because they were substantively unreasonable, but because it was unreasonable to rely on them where the other party had not known about their existence or did not comprehend their effect.

This ground can be more accurately described as "unfair surprise".[2]

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1 Ibid., 95.

2 See, generally, Trebilcock, op. cit., 370-373. Also J.A. Spanogle, Analyzing Unconscionability Problems (1969) 117 U. Pa. L.Rev. 931.

So phrased it becomes clear that the test relates to terms which the promisee was unaware of, or which were misleading or incomprehensible to the layman. Unfair surprise, however, presupposes that the non-drafting party entertains certain expectations in respect of the contract and, therefore, before a court can strike down a clause on that basis it has to determine (a) whether the party's expectations were reasonable in the circumstances, and (b) whether the actual terms were substantially at variance with these expectations.[1] In the cases discussed these matters were not clearly examined.

Another important question raised by the recognition of unfair surprise as a ground for striking down a clause, is whether a certain degree of notification will be sufficient to insulate an unfair clause from attack. In the cases reviewed this problem did not arise. Yet in Gillespie Bros., Lord Denning did indicate that a clause will only be given effect to if it is agreed and reasonable. In the Levison case it would seem as if the Master of the Rolls regarded the terms as oppressive, onerous and one-sided in that they required of Levison to bear, except for a small amount, all the risk, while the cleaners undertook very limited obligations in return. This is clearly a very difficult problem which will depend upon judicial policy vis-à-vis certain terms and a balancing of the parties' interests. It is submitted that although there will obviously be clauses which are objectionable per se, such as those which, purely to hinder a party

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[1] See Trebilcock, op. cit., 370.

in the exercise of his rights, require of him to submit to foreign jurisdiction in the case of disputes, a clause which is known and understood will only rarely be struck down.

If, therefore, a clause can be insulated from attack by notification, what degree of notification will suffice? Is it enough if the non-drafting party merely reads the contract terms or must he also understand them? The courts have, in the past, used strict rules relating to the incorporation of documents as a method of denying consent to unfair exemption clauses. However, the problem of unfair surprise may arise even where a term has technically been consented to. It is therefore necessary for the proper application and functioning of the test of unfair surprise that clear criteria be laid down.

6 - INEQUALITY OF BARGAINING POWER

Following his statement in Gillespie Bros. & Co.Ltd. v. Roy Bowles Transport Ltd., Rennie Hogg Ltd.[1] that contract terms may be struck down if they are unreasonable, Lord Denning has suggested more recently that English law permits a court to grant relief from unfair or unreasonable contracts which were concluded by parties between whom there was great inequality of bargaining power.

The principle was first enunciated in Lloyds Bank Ltd. v. Bundy:[2] Mr. Bundy was an elderly farmer and had but one main asset, his farmhouse, worth £10,000. Out of affection for his only son he charged his house for £11,000 as a guarantee for the repayment of debts owed by his son's company to the bank. Eventually the company went into receivership and the bank sought to enforce its rights as mortgagee. Bundy's defence was that he had executed the charge under the influence of the bank manager and that he had no-one else to advise him on the transaction. The majority of the Court of Appeal (Cairns L.J. and Sir Eric Sachs) set aside the transaction on the ground of undue influence. Sir Eric Sachs accepted the proposition that Bundy had relied on the bank manager for advice and concluded that there was a relationship of confidentiality between them. As the manager knew that the company's position was precarious and that Bundy could lose everything he had, but had not advised him accordingly, the duty of care which arises from such a relationship was not discharged.

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1 [1973] Q.B. 400, 416-417.

2 [1975] 1 Q.B. 326.

Lord Denning M.R. based his decision on other grounds. He said that although "/n/o bargain will be upset which is the result of the ordinary interplay of forces"[1] there are exceptional cases in which the courts will set aside a contract or a transfer of property when the parties have not met upon equal terms - "when the one is so strong in bargaining power and the other so weak - that, as a matter of common fairness, it is not right that the strong should be allowed to push the weak to the wall."[2] These cases are divided into separate categories: duress of goods, unconscionable transactions with the weak and necessitous, undue influence, undue pressure and unfair salvage agreements.

> Gathering all together, I would suggest that through all these instances there runs a single thread. They rest on 'inequality of bargaining power'. By virtue of it, the English law gives relief to one who, without independent advice, enters into a contract upon terms which are very unfair or transfers property for a consideration which is grossly inadequate, when his bargaining power is grievously impaired by reason of his own needs or desires, or by his own ignorance or infirmity, coupled with undue influences or pressures brought to bear on him by or for the benefit of the other. When I use the word 'undue' I do not mean to suggest that the principle depends on proof of any wrongdoing. The one who stipulates for an unfair advantage may be moved solely by his own self-interest, unconscious of the distress he is bringing to the other. I have also avoided any reference to the will of the one being 'dominated' or 'overcome' by the other. One who is in extreme need may knowingly consent to a most improvident bargain, solely to relieve the straits in which he finds himself. Again, I do not mean to suggest that every transaction is saved by independent advice. But the absence of it may be fatal.[3]

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1 Ibid., 336.

2 Ibid.

3 Ibid., 339.

Applying these principles to the case in hand Lord Denning held (1) that the transaction constituted a grossly unequal exchange: while the bank gained security of £11,000 neither Bundy nor his son's company got anything in return, (2) the relationship between the bank and Bundy was one of trust and confidence, and (3) Bundy was motivated to conclude the transaction out of affection for his son.[1]

Since Lloyds Bank Ltd. v. Bundy, Lord Denning has applied the principle of inequality of bargaining power in a number of dissimilar factual settings. In Arrale v. Costain Civil Engineering[2] the Master of the Rolls said that a release of a tort claim for no consideration by a poor labouring Arab should be set aside on the ground that it was done when his bargaining power was impaired by reason of his own ignorance. Although he signed the release in the presence of a lawyer friend he did so without the effect of the release being explained to him. Lord Denning added that no misconduct could be attributed to the defendant's representative.[3]

The principle has also been applied in the context of standardized agreements. In Clifford Davis Management Ltd. v. W.E.A. Records,[4] where two songwriters had bound themselves to assign the copyright in their compositions to their manager, Lord Denning referred to the case of A. Schroeder Music Publishing Co.Ltd. v. Macaulay[5] as supporting the principle of unequal bargaining power and held that the following factors

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1 Ibid., 339-340.

2 [1976] 1 Ll.Rep. 98.

3 Ibid., 102.

4 [1975] 1 W.L.R. 61.

5 [1974] 1 W.L.R. 1308.

made out a case of inequality of bargaining power:[1] (a) The fact that the songwriters had tied themselves for a period of 10 years without getting a retaining fee and with no promise in return other than that the manager should use his best endeavours to get the compositions published. (b) The copyright was turned over for a grossly inadequate fee. (c) The songwriters' bargaining power was impaired by the fact that they wished to get their work published and that they were dependent upon the manager in order to do so. (d) Undue pressure and influences were brought to bear on the composers. They had to sign long and complicated standard forms which they did not understand and they had to do so without advice. In the already discussed[2] Levison v. Patent Steam Carpet Cleaning Co.Ltd.[3] Lord Denning also purported to apply the principle of unequal bargaining power.

A principle similar to that set out in Lloyds Bank Ltd. v. Bundy has been widely applied in Canada. The cases, which date back as far as the late nineteenth century[4] seem to operate on the same principles on which the Chancery courts gave relief from agreements in which one party had unfairly taken advantage of or exploited a bargaining handicap of another to the latter's detriment. Bradley Crawford, commenting on the cases in 1966, said that

> ... the courts intervene to rescind the contract whenever it appears that one of the parties was incapable of adequately protecting his interests and the other has made some immoderate gain at his expense.[5]

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1 /1975/ 1 W.L.R. 61, 65.

2 Ante, 293.

3 /1977/ 3 W.L.R. 90.

4 See, for example, Waters v. Donnelly (1884), 9 O.R. 391.

5 Comment (1966) 44 Can. Bar Rev. 142, 143.

So, for example, where a woman, in acute emotional and mental anxiety and strain because of a pending divorce, signed away her half-share in certain property and relinquished her claim to alimony, the court set aside the transaction on the ground of the inequality of the parties in respect of the task of protecting their respective interests, and the improvidence of the transaction.[1] In Paris v. Machnick,[2] the court adjusted a contract whereby an illiterate woman had sold land worth $9,000 for $2,500. The court held the woman had no idea of the value of the property nor any real understanding of the consideration that was paid to her. These principles have been applied to a variety of contract types such as sales of land,[3] moneylending transactions,[4] releases of damage claims,[5] and a contract for dancing lessons.[6] The parties who have merited such protection include the old, the poor, the ignorant and people of limited intelligence.

What is the nature of the doctrine espoused by Lord Denning and applied in the Canadian courts? Although in Lloyds Bank Ltd. v. Bundy Lord Denning provided a number of categories which, he claimed, supported his principle of inequality of bargaining power, it is, in my view, largely a resuscitation of Chancery's doctrine in terms of which relief

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1 Mundinger v. Mundinger (1969) 3 D.L.R. (3d) 338 (Ont. C.A.)

2 (1973) 32 D.L.R. (3d) 723 (N.S.C.T.D.)

3 Mundinger v. Mundinger (1968) 3 D.L.R. (3d) 338 (Ont.C.A.); Paris v. Machnick (1973) 32 D.L.R. (3d) 723 (N.S.C.T.D.)

4 McKenzie v. Bank of Montreal (1975) 55 D.L.R. (3d) 641 (Ont.H.C.)

5 Pridmore v. Calvert (1975) 54 D.L.R. (3d) 133 (B.C.S.C.)

6 Gaertner v. Fiesta Dance Studios Ltd. (1973) 32 D.L.R. (3d) 639.

was given from unconscionable contracts entered into by weak and necessitous parties. A few years before the Bundy case this doctrine of equitable fraud was applied in Creswell v. Potter,[1] where a woman in the process of divorce signed a release of her interest in certain property for inadequate consideration. Megarry J. relied on the statement by Kay J. in Fry v. Lane[2] that the court will set aside a purchase made from a poor and ignorant person at a considerable undervalue, the seller having no independent advice. In Backhouse v. Backhouse[3] the court described Creswell v. Potter as possibly falling within the principle of inequality of bargaining power as set out by Lord Denning.

The operation of the principle of inequality of bargaining power is dependent upon three factors: firstly, that the disadvantaged party suffered from a bargaining handicap which made him vulnerable to exploitation or which made him unable to protect his own interests. In Lloyds Bank Ltd. v. Bundy this requirement was fulfilled by the fact that Bundy, apparently inexperienced in commercial matters, implicitly relied on the bank manager for guidance and in Arrale v. Costain Civil Engineering by the fact that the person was, because of his station in life, unable to understand the purport of the release which he signed. Lord Denning has also assumed inequality of bargaining power to exist where one party contracted with another on the basis of the latter's printed terms of business.[4] In such circumstances, it will often be

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1 Decided in 1968, but reported only in [1978] 1 W.L.R. 255.

2 (1888) 40 Ch.D. 312, 322.

3 [1978] 1 W.L.R. 243.

4 Clifford Davis Management Ltd. v. W.E.A. Records [1975] 1 W.L.R. 61; Levison v. Patent Steam Carpet Cleaning Co.Ltd. [1977] 3 W.L.R. 90.

obvious that there is an imbalance in economic power between the parties. That does not, however, mean that a court can assume that a contract or clause was the product of inequality of bargaining power caused by market concentration. Such an inference can only be drawn after a wide-ranging inquiry as to the alternative sources of supply available to a party. As I have argued before, the courts are hardly qualified to undertake an inquiry of that scope. A judicially applied principle of inequality of bargaining power can operate in isolated cases to redress unfairness which can be explained by or traced to a specific bargaining weakness in one party, but it cannot undertake a task as comprehensive as correcting imbalances which are inherent to the social and economic system.

Secondly, relief will only be given where the terms are very unfair or where there is a gross disparity in the value of the respective performances. While the recent cases have provided little indication of the required degree of disparity the Chancery cases generally gave relief where the imbalance was to the ratio of 2 to 1. However, such a standard provides a guideline only where the unfairness relates to price or related clauses and not where the contract terms are generally one-sided or oppressive. In Lloyds Bank Ltd. v. Bundy Lord Denning listed a third requirement namely, that there must have been "undue influences or pressures brought to bear ... by or for the benefit of the other."[1] It is, however, clear from Lord Denning's statement that, as was the case under equitable fraud, it is not necessary to

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[1] [1975] 1 Q.B. 326, 339.

prove this conclusively. It is merely insisted on in order to provide a causal link between the bargaining handicap of the one party and the unfair contract and where these requirements are proved the court will infer from them that the weaker party has been taken advantage of or has been exploited. The Arrale case clearly indicated that relief would be given even if there was no misconduct on the part of the defendant.

An agreement which is substantively unfair may still be upheld if the disadvantaged party had independent advice. Nevertheless, the presence of such an adviser is, as the Arrale case shows, and Lord Denning intimated in Lloyds Bank Ltd. v. Bundy, by no means conclusive.

The doctrine of inequality of bargaining power is a valuable weapon against unfair contracts. It is not a novel doctrine, but is firmly based on principles developed in the Chancery courts since the late seventeenth century. However, its application is by necessity restricted to cases where a specific bargaining handicap distorts the market. It is not a mechanism through which the courts can attempt to redress the inequalities inherent in the social and economic structures.

The doctrine of unequal bargaining power, as set out by Lord Denning, has not been applied in Scotland. Although it is based on principles peculiar to English law there is no reason why extortion, facility and circumvention and undue influence cannot be combined and restated in the form of a doctrine of unequal bargaining power by an innovative court.[1]

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[1] See the recommendation by the Scottish Law Commission in Memorandum No. 42, Defective Consent and Consequential Matters, paras. 3.120-3.132 that a new ground for relief called "lesion" be recognised in Scotland.

PART II

1 - MONEYLENDING AND CREDIT AGREEMENTS:

A STATUTORY REQUIREMENT OF FAIRNESS

The repeal of the usury laws in 1854 left the borrower unprotected and at the mercy of the moneylender. The ensuing exploitation of borrowers by unscrupulous moneylenders became so serious that Parliament intervened and put the Moneylender Act 1900 on the statute book. This Act and the Moneylender Act 1927 came into force in both Scotland and England.

a) The Moneylenders Acts of 1900 and 1927[1]

The Moneylender Act of 1900 provided that where there was evidence that the interest charged by a moneylender[2]

> in respect of the sum actually lent is excessive, or that the amounts charged for expenses, inquiries, fines, bonus, premium, renewals, or any other charges are excessive, and that, in either case the transaction is harsh and unconscionable or is otherwise such that a court of equity would give relief[3]

the court may reopen the transaction. This section was modified by section 10 of the Moneylenders Act 1927 which laid down a rebuttable presumption that interest at a rate of more than 48 per cent per annum was excessive within the terms of the Act. If the court found

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1 See, generally, Bellot, The Legal Principles and Practice of Bargains with Money-lenders; Meston on Moneylenders.

2 According to section 6 "moneylenders" includes "every person whose business is that of moneylending, or who advertises or announces himself or holds himself out in any way as carrying on that business." See, however, the exceptions mentioned in section 6(a) - (e).

3 Section 12 of the Act of 1927 made illegal any agreement that the borrower should pay any sum on account of costs, charges or expenses relating to the negotiations for or the granting of the loan.

a transaction to be harsh and unconscionable it had wide powers of relief: it might

> relieve the person sued from payment of any sum in excess of the sum adjudged by the court to be fairly due in respect of such principal, interest and charges, as the court, having regard to the risk and all the circumstances, may adjudge to be reasonable; and if any such excess has been paid, or allowed in account, by the debtor, may order the creditor to repay it; and may set aside, either wholly or in part, or revise, or alter, any security given or agreement made in respect of money lent by the moneylender, and if the moneylender has parted with the security may order him to indemnify the borrower or other person sued.[1]

The power of control which the Act conferred on the courts was not uniformly welcomed by the judges[2] and in England the section was initially narrowly interpreted as merely entrenching in statute the jurisdiction which Chancery had already developed earlier in order to protect weaker parties against exploitation.[3] This was soon seen to be an excessively restricted view and in Re Debtor, ex parte The Debtor[4] it was held that the jurisdiction conferred by the Act was new and was not confined to cases in which courts of equity would have intervened before the Act. Such a view was strengthened by the facts that under the Act the courts had the power to make new agreements for the parties which they never had under the limited jurisdiction of equity and that the Act also applied in Scotland where Chancery's jurisdiction was unknown.

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1 Section 1. Section 1(4) provided that "/t/he foregoing provisions of this section shall apply to any transaction which, whatever its form may be, is substantially one of moneylending by a moneylender."

2 See, for example, Channel J.'s remarks in Barnett v. Corunna, The Times, 16th June, 1902, as quoted by Bellot, op. cit., 264.

3 Wilton & Co. v. Osborne /1901/ 2 K.B.110.

4 /1903/ 1 K.B.705, approved in Samuel v. Newbold /1906/ A.C. 461 (H.L.).

From the start, however, the courts applied their newly gained power with circumspection. Following the Act they pinpointed the following situations as justifying the "reopening" of a transaction: (i) where the remuneration was excessive and the transaction harsh and unconscionable, and (ii) where the remuneration was excessive and the transaction otherwise such that a court of equity would give relief. In practice there was no distinction between these situations and the same circumstances could lead to intervention on either ground.

In general, the courts were unwilling to give relief merely because the remuneration was out of proportion to the sum advanced and the risk incurred. According to Vaughan Williams L.J. in Poncione v. Higgins

> /T/he intention of the Legislature was to deal with cases of persons in financial distress coming to moneylenders to borrow money in order to get out of their financial distress, which was often urgent and pressing, and not to deal with the case of persons who were in a position to make their own bargain on terms of equality with the money-lender. The Legislature threw upon the money-lender who chose to advance money to persons in financial distress the obligation not to take advantage of their distress or their incapacity to negotiate.[1]

The approach envisaged was, therefore, one with which the English courts, through the well-known equity jurisdiction, were well acquainted. In the same case Cozens-Hardy L.J. held that to answer the question whether a transaction should be reopened

> /t/he circumstances of each case must be considered, including the necessities of the borrower, his pecuniary

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1 (1904) 21 T.L.R. 11, 12.

> position, the presence or absence of security, the relation in which the moneylender stood to the borrower, and the total remuneration derived by the moneylender from the whole transaction.[1]

In this enquiry the risk that the moneylender was running in advancing the money was of extreme importance. Where sufficient security was given the courts were loath to allow a high rate of interest. And even where the advance was unsecured, but the moneylender was aware that the borrower had ample property to cover the loan and was a good man to do business with,[2] the rate of interest allowed would be lower than where the risk was high. Another factor which had considerable influence on the question whether a transaction would stand or not was the presence of a default clause,[3] especially where the precise effect of such a clause was not fully understood by the borrower.[4] Where there was active unfair dealing by the moneylender during the negotiation such as misstatements[5] or not explaining a transaction which he knew the borrower did not understand,[6] the finding that the transaction was harsh and unconscionable would be all the more emphatic. But it is extremely doubtful whether it was necessary, as Lord McLaren maintained in Midland Discount Co. v. Macdonald, to prove "some fault on the part of the moneylender,

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1 (1904) 21 T.L.R. 11, 12.

2 Samuel v. Newbold [1906] A.C.461, 475 per Lord James.

3 Section 7 of the Act of 1927 prohibited any contract for the payment of compound interest "or for the rate or amount of interest being increased by reason of any default in the payment of sums due under the contract".

4 Levene v. Greenwood (1904) 20 T.L.R.389.

5 Victorian Daylesford Syndicate Ltd. v. Dott (1905) 21 T.L.R.742.

6 Levene v. Greenwood (1904) 20 T.L.R.389; Wells v. Joyce [1905] 2 I.R.134.

some want of fairness in the transaction for which he may justly be held responsible.[1] At most it was required that the moneylender had knowledge of the weakness, folly or necessity of the borrower and often even this requirement was dispensed with.

In some exceptional cases the courts were even prepared to depart from their general rule and give relief on the ground of excessive remuneration per se. Where a very high rate of interest was charged the technique used was to place on the moneylender the burden of showing that despite the excessive interest rate the transaction was in fact fair and reasonable.[2] In other cases the courts were prepared to infer solely from the exorbitant rate of interest that the borrower was not fit to do business and that the transaction was therefore harsh and unconscionable within the Act.[3] Where the rate of interest was clearly exorbitant, for example, a few hundred per cent per year, such an approach was perhaps justified.

Section 1 of the 1900 Act gave the court wide powers of relief where it has found a transaction to be harsh and unconscionable. Unlike the equity courts which could only set aside an unconscionable agreement the courts could create an entirely new contract between the parties. In general, the courts set aside the transactions and ordered repayment of the principal sum lent plus reasonable interest.

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1 1909 S.C. 477, 484.

2 Ibid., 467 per Lord James. See also Debenham Ltd. v. McCall 1923 S.L.T.365 where an interest rate of 300 per cent per year was found to be harsh and unconscionable because the moneylender could not explain or justify the unreasonable nature of the transaction.

3 See, for example, the suggestion to that effect in Saunders v. Newbold [1905] Ch.260.

In conclusion, it is clear that the courts, in applying the statutory test of fairness, depended largely on the principles which governed Chancery's jurisdiction against equitable fraud. While paying lip service to the idea that parties were free to conclude any agreements they wished and that relief would only be given where there was evidence to show active overreaching of the borrower by the lender they have in the main adopted a more objective approach.

b) Consumer Credit Act 1974[1]

As a measure of consumer protection the value of the Moneylenders Acts was limited by the fact that the power of the courts to reopen transactions was restricted to those which fell within the scope of the Acts. Large areas of consumer credit such as hire-purchase or instalment sale contracts were excluded from the jurisdiction.[2] In addition, the fact that lenders could often justify a high rate of interest in terms of risk or the smallness of the amount advanced, made borrowers reticent to defend themselves in terms of the Act.

To obviate these problems and to consolidate and unify the law relating to credit transactions in a single Act the Legislature passed the Consumer Credit Act 1974.

Although the Moneylenders Acts of 1900 and 1927 are still in force it is expected that they will soon be superseded as the Consumer

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1 See, generally Goode, Introduction to the Consumer Credit Act 1974.

2 Ibid., 1-6.

Credit Act 1974 provides that the Secretary of State for Prices and Consumer Protection may by statutory instrument repeal the Moneylenders Acts.[1]

Sections 137-140 confer on the courts wide powers to reopen a credit agreement where it is found that a credit bargain is extortionate. A "'credit agreement' means any agreement between an individual ('the debtor') and any other person ('the creditor') by which the creditor provides the debtor with credit of any amount."[2] The power to reopen therefore extends to all credit agreements except hiring agreements, for which separate provision is made.[3] The transaction which may be reopened is the credit agreement, but in order to do so the court must examine the credit bargain. The latter includes not only the credit agreement but also such other transactions which must be "taken into account in computing the total charge for credit."[4]

In terms of section 138(1) a credit bargain is extortionate if it:

> (a) requires the debtor or a relative of his to make payments (whether unconditionally, or on certain contingencies) which are grossly exorbitant, or
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> (b) otherwise grossly contravenes ordinary principles of fair dealing.

The words "(whether unconditionally, or on certain contingencies)" make it clear that the scrutiny of the court extends not only

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1 Section 192(4).

2 Section 137(2)(b)(i).

3 Section 132.

4 Section 137(2)(b)(ii).

to the primary obligations of the debtor but also to stipulations relating to default. It is furthermore significant that unlike the Moneylenders Acts which did not expressly permit such a possibility - although it was interpreted by the courts as being possible - the Consumer Credit Act, by employing the word "or" expressly recognises that mere exorbitancy of the payment to be made may render a contract extortionate within the terms of the Act.

In determining whether a credit bargain is extortionate, section 138(2) prescribes that

> regard shall be had to such evidence as is adduced concerning -
> (a) interest rates prevailing at the time it was made,
> (b) the factors mentioned in subsections (3) to (5), and
> (c) any other relevant considerations.

The factors which in terms of section 138(3) are applicable under subsection (2) in relation to the debtor include -

> (a) his age, experience, business capacity and state of health, and
> (b) the degree to which, at the time of making the credit bargain, he was under financial pressure, and the nature of that pressure.

And the factors which according to section 138(4) are applicable to the creditor include -

> (a) the degree of risk accepted by him, having regard to the value of any security provided;
> (b) his relationship to the debtor; and
> (c) whether or not a colourable cash price was quoted for any goods or services included in the credit bargain.

Section 138(5) provides that the

> factors applicable under subsection (2) in relation to a linked transaction include the question how far the transaction was reasonably required for the protection of debtor or creditor, or was in the interest of the debtor.

The court is only <u>obliged</u> to consider the factors mentioned above on which evidence has been adduced.[1] It is also important to

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[1] Section 138(2)

note that the factors listed in section 138(2) are merely inclusive and are thus not the only factors which may be taken into account. Those factors which have been singled out for specific mention largely correspond to the factors which the courts have considered in deciding whether an agreement is to be reopened under the Moneylenders Acts.

The court may not mero motu reopen a credit agreement. It may only do so at the instance of either the debtor or a surety. Section 171(7) furthermore provides that if, in proceedings referred to in section 139(1), the debtor or surety alleges that the credit bargain is extortionate it is for the creditor to prove the contrary.

In reopening the agreement, the court may, for the purpose of relieving the debtor or surety from payment of any sum in excess of that fairly due and reasonable, by order:

> (a) direct accounts to be taken, or (in Scotland) an accounting to be made, between any persons,
> (b) set aside the whole or part of any obligation imposed on the debtor or a surety by the credit bargain or any related agreement,
> (c) require the creditor to repay the whole or part of any sum paid under the credit bargain or any related agreement by the debtor or a surety, whether paid to the creditor or any other person,
> (d) direct the return to the surety of any property provided for the purposes of the security, or
> (e) alter the terms of the credit agreement or any security instrument. [1]

Such an order may be made by the court "notwithstanding that its effect is to place a burden on the creditor in respect of an advantage unfairly enjoyed by another person who is a party to a linked transaction."[2]

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[1] Section 139(2).

[2] Section 139(3).

2 - EXEMPTION CLAUSES: A STATUTORY REASONABLENESS REQUIREMENT

It has long been recognised that exemption clauses are a source of actual or potential injustice. To the promisee, who is often unaware of the existence and meaning of these clauses, their invocation means that the value of his bargain and the remedies available to or against him are substantially dissimilar from what he expected. And even where the promisee knows of an exemption clause and comprehends its effect he may find that he is unable to locate a supplier who will contract on the basis of materially different terms. In addition, by exempting a party from liability for his own negligence or breach such a clause may promote inefficiency.

In view of these factors it was, therefore, hardly surprising that the courts regarded exemption clauses with disfavour and attempted to restrict their effectiveness where they were perceived to operate unfairly. The various techniques employed and their shortcomings have been reviewed before. It will suffice to say here that the main problem was that although the use of those techniques was impelled by considerations of fairness their focus was on other matters. The effect was, therefore, not only to distort the principles involved, but also to make the controls inflexible and arbitrary, and thereby to create uncertainty. The one instrument of control which attempted to deal directly with the undercutting effect which exemption clauses have on a party's expectations, namely the substantive doctrine of fundamental breach, was beset by conceptual problems. In addition, its application had become uncertain as a result of the statements made in Suisse Atlantique[1] and

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[1] /1967/ 1 A.C. 371.

the interpretation of those *dicta* in subsequent cases.[1] The alternative and more direct approach of subjecting exemption clauses to a reasonableness test was suggested by Lord Denning in a few cases, but on the whole the courts were unwilling to follow this lead. It was thus necessary for the legislature to intervene and confer on the courts the power to test the reasonableness of exemption clauses.

Until recently, the only situation in which the courts had been given a statutory power to police exemption clauses for reasonableness was in relation to carriage by railway: section 7 of the Railway and Canal Traffic Act. More than a century was to pass before the legislature, by section 3 of the Misrepresentation Act 1967, again conferred on English courts the power to test an exemption clause for reasonableness. Despite the criticism attracted by the method of control proposed in that Act, Parliament in 1973 passed the Supply of Goods (Implied Terms) Act, which laid down a similar test for terms which purport to restrict the liability for breach of a seller or owner's implied obligations in contracts of sale of goods and of hire-purchase. A judicially administered test of reasonableness was introduced over a much wider area in the Unfair Contract Terms Act 1977. The provisions relating to implied undertakings in sales and hire-purchases have been repeated in, and to some extent amended by, the 1977 Act and will be discussed under that Act.

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[1] See, for example, Harbutt's "Plasticine" Ltd. v. Wayne Tank Co.Ltd. [1970] 1 Q.B. 447.

(a) The Railway and Canal Traffic Act 1854[1]

During the late eighteenth and early nineteenth centuries, common carriers were subjected to strict control by the common law: not only were they obliged to carry goods offered to them for a reasonable remuneration, but they were also held strictly liable for any loss or damage in relation to the goods which they carried. Not unnaturally, they attempted to exclude this liability by putting up notices to that effect. The Carriers Act of 1830 somewhat restricted this practice, but left the carrier otherwise free to limit or exclude his liability under a "special contract." Towards the middle of the nineteenth century the railway had become almost the only mode of inland transport. This monopolistic position was used to conclude "special contracts" with the consignors in which they drastically cut down the liabilities which attached to them as common carriers. This practice led to grave injustice and Parliament responded by passing the Railway and Canal Traffic Act in 1854.

Section 7 of that Act held carriers by railway liable for any loss or injury to the goods carried by them and caused by the neglect or default of the carriers or their servants. However, special contracts limiting such liability in relation to the receiving, forwarding and delivering of the goods were to be valid, but only if the court adjudged them to be "just and reasonable".

The phrase "just and reasonable", of course, had no meaning in itself and its content was entirely dependent upon judicial interpretation, a fact which was by no means welcomed by all judges.[2] However,

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1 See, generally, Kahn-Freund, Law of Carriage by Inland Transport, 214-228.

2 See, for example, Pardington v. South Wales Railway Co. (1856) 1 H. & N. 392.

eventually the House of Lord decided in Peek v. North Staffordshire Railway Co.,[1] that the exempting conditions had to be contained in a document signed by the consignor and they had to be just and reasonable. They furthermore maintained that a special contract containing conditions limiting or excluding the liability of the carrier would be just and reasonable if the consignor had also been offered a "fair alternative". That meant that the consignor had to be given the option of contracting at his own or at the company's risk. In addition, it was declared that such an alternative would only be fair if the consignor who chose to bear the risk himself was offered a lower rate than he would have had to pay if the carrier had assumed the risk, or if the consignor was offered some other advantage.

The availability of a "fair alternative" subsequently became the central factor in determining whether the exempting conditions were reasonable or not. Such an interpretation of section 7 was entirely consistent with the principle of freedom of contract, because it focussed on the formation of the contract rather than on the substantive reasonableness of the contract. Provided the consignor had a genuine choice of alternatives the contract would be regarded as reasonably made. And so long as the contract was made in a just and reasonable manner, the contract itself was deemed just and reasonable.[2]

During the twentieth century the railways lost its earstwhile monopoly in respect of inland transport and in 1962 the Transport Act

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1 (1863) 10 H.L.C. 473.

2 Atiyah, The Rise and Fall of Freedom of Contract, 559. See also Brown v. Manchester, Sheffield & Lincolnshire Railway (1883) 8 App.Cas. 703, 716.

repealed the Railway and Canal Traffic Act. Section 7, however, not only had an important effect on the manner in which transport law developed, but the relative success with which it was applied, also paved the way for the enactment of reasonableness tests in other areas of contract law.

(b) The Misrepresentation Act 1967

Section 3 of the Misrepresentation Act has now been re-written by the Unfair Contract Terms Act 1977.[1] It reads as follows:

> If a contract contains a term which would exclude or restrict -
> (a) any liability to which a party to a contract may be subject by reason of any misrepresentation made by him before the contract was made; or
> (b) any remedy available to another party to the contract by reason of such a misrepresentation,
> that term shall be of no effect except in so far as it satisfies the requirement of reasonableness as stated in section 11(1) of the Unfair Contract Terms Act 1977; and it is for those claiming that the term satisfies that requirement to show that it does.

Section 11(1) of the Unfair Contract Terms Act specifically provides that in order to determine whether a term complies with the test of reasonableness regard must be had to the time when the contract was concluded. A main source of criticism[2] of the earlier version of section 3 was that no guidelines for the application of the reasonableness test had been provided. It would, however, now seem as if the guidelines contained in section 11(4) of the Unfair Contract

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1 Section 8(1).

2 See, for example, P.S. Atiyah and G.H. Treitel, Misrepresentation Act 1967 (1967) 30 Mod.L.Rev. 369, 384-385.

Terms Act are, by virtue of the words "or any other Act", also applicable to section 3. The Misrepresentation Act does not apply to Scotland.

(c) The Unfair Contract Terms Act 1977[1]

The provisions of the Act largely follow the recommendations of the Law Commissions of Scotland and England.[2] The law relating to England and Scotland is set out separately in Parts I and II respectively. In the following discussion the English and Scots provisions have been, wherever possible, discussed simultaneously. In terms of the Act some exemption clauses are completely ineffective and others are subject to a reasonableness test.[3] The former provisions are beyond the scope of this work.

The controls contained in the Act are wide, but they do not apply to all exemption and related clauses: the operation of the Act is dependent upon the status of the parties, the nature of the liability or obligation affected and the type of contract in which they are contained.[4]

The Act has been firmly drafted on the premise that freedom of contract should not be unduly disturbed. With the exception of the

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1 See, generally, Rogers and Clarke, The Unfair Contract Terms Act 1977; Treitel, Law of Contract, 179-193; F.M.B. Reynolds, The Unfair Contract Terms Act 1977 [1978] 2 LMCLQ 201; B.Coote, Unfair Contract Terms Act 1977 (1978) 41 Mod.L.Rev. 312.

2 The Law Commission and the Scottish Law Commission [hereafter the Joint Law Comm.] Exemption Clauses, Second Report.

3 Part I of the Act also deals with non-contractual notices, for example, in sections 2 and 11(3). These fall outside the scope of this work.

4 Coote, op. cit., 312. In Scotland the main controls of the Act apply only to the types of contract listed in section 15(2). There is no corresponding provision in Part I.

limited areas in which exclusion clauses are made completely ineffective, there has been little attempt to impose any "minimum decencies" on the contract. The exceptions that have been made apply mostly where one party to the contract is a consumer. They have been singled out for special treatment because they are regarded as having limited bargaining power, and are, therefore, more vulnerable to exploitation. It was felt that where both parties to a contract act in the course of a buiness[1] should be left free to regulate their affairs according to the dictates of commercial expediency. It may perhaps be questioned whether the assumption as to the equal bargaining strength of business parties[2] is always as justified as it is made out to be. It would, perhaps, have been better to have left any decisions on that point for the court to make on the basis of the particular contingencies of the case rather than to have disposed of the matter a priori on the basis of status. However, even between business parties the test of reasonableness will still have to be complied with. The danger may be that the courts, in applying the test, will make their decision with reference only to the assumed equality of bargaining power between the parties and not by considering the substantive fairness of the term in question. It is, after all, implicit in the Act that an exemption clause may still be reasonable even if it deprives a party completely of his contractual or delictual remedies.[3]

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1 An exception has been made in sections 2(1) and 16(1) which render ineffective a clause restricting liability for death or personal injury caused by negligence or breach of a duty, irrespective of whether both parties act in the course of a business.

2 Joint Law Comm., op. cit., para. 147.

3 Cf. section 2-719 of the Uniform Commercial Code which prohibits the total exclusion of a promisee's remedies.

The Law Commissions[1] were clearly aware of the controversy about whether exemption clauses prevent the accrual of obligations or operate as defences to accrued rights of action,[2] and some provisions of the Act are expressly drafted to cover clauses which purport only to define a party's obligation.[3] On the whole the Act has proceeded on the assumption that exemption clauses operate as defences to liability incurred.[4] To have held otherwise, would have necessitated legislation dealing not with the reasonableness of exemption clauses but with the reasonableness of the contract. That might indeed have been the better approach. On the other hand, it has been validly argued that at least in the case of standard contracts, the approach of the Act is justified in view of the fact that the contracting party has certain reasonable expectations, arising from the type of contract involved, which should not be detracted from by exemption clauses or by careful drafting on the part of the promisor.[5]

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1 Op. cit., paras. 143-144.

2 See Coote, Exception Clauses.

3 See, for example, sections 3, 17, 13(1) and 25(5).

4 This has led to severe criticism from some commentators, for example, Coote, (1978) 41 Mod.L.Rev. 312 et seq.

5 See, for example, the argument by J. Adams, An Optimistic Look at the Contract Provisions of Unfair Contract Terms Act 1977 (1978) 41 Mod. L.Rev. 703, 704 that standard form contracts should not necessarily be subjected to the same rules as negotiated contracts.

(i) Scope and Application

Commercial contracts:

The main controls of the Act apply only where a clause restricts or excludes liability for breach of obligations or duties arising in the course of business or from the occupation of premises used for business purposes.[1] "Business", although not defined in the Act, includes the professions, government departments and local or public authorities.[2] The Law Commissions were of the opinion that the equality of bargaining power between private parties and the rarity of exemption clauses in "private contracts" made it unnecessary to extend the proposed controls to such contracts.[3] Whether such a view was justified will depend largely on how widely the term "business" is interpreted by the courts.

Consumer contracts:

The operation of the Act is also in some cases made dependent upon one party dealing, and the other not dealing in the course of a business.[4] In the case of contracts for the supply of goods there is a further requirement that the goods must be of a type ordinarily supplied for private use or consumption.[5] In Rasbora Ltd. v. J.C.L.Marine Ltd.[6] it was held under the similar provision in section 55(7) of the

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1 Sections 1(3), 16, 17, 18.

2 Sections 14 and 25(1).

3 Op. cit., para. 9.

4 Sections 12(1)(a), 12(1)(b) and 25(1).

5 Section 12(1)(c) and 25(1).

6 [1977] 1 Ll.Rep.645.

amended Sale of Goods Act 1893, that a sale to a company can be a consumer sale if the company was set up for the purpose of acquiring the goods and they were for the sole consumer use of the members of the company. In addition, the court held that a sale which was originally a consumer sale would remain so even if, as a result of novation, a buyer who is a non-consumer, is substituted.

Standard form contracts:

In one situation the operation of the Act is made dependent upon a "business" party dealing on the other's "written standard terms of business" or on the contract being a standard form contract.[1] Following the recommendations of the Joint Law Commissions these terms have not been defined.[2] Attempts have been made in other countries to define standardized contracts, but these have never been entirely successful and it was thought that it would be better to leave it to the courts to decide whether a contract qualified or not. Problems may occur about the extent of negotiation which will be sufficient to take a contract out of this category.

Neither Scots nor English law has previously attempted to isolate specific categories of contract by reference to their factual settings, and subjected them to special rules.[3] It is submitted that

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1 Sections 3 and 17.

2 Op. cit., paras. 151-157.

3 See, however, J.P. Dawson, Unconscionable Coercion - The German Version (1976) 89 Harv.L.Rev. 1041, 1103, who asserts that German law has for a long time treated standard form contracts differently from negotiated contracts.

this, rather than the normal monolithic approach, is in principle, a better way of dealing with problems which may involve different policy considerations in different contexts.

Types of clauses affected:

The Act sets out to control clauses which "exclude or restrict" the liability of the promisor. Such clauses include those which seek to do so by imposing conditions on enforcement, or by excluding or restricting rights or remedies, or the rules of evidence and procedure.[1] The Act, furthermore, provides that the controls proposed in certain specified sections also apply to exclusions and restrictions of liability by reference to terms and notices which exclude or restrict the relevant duty or obligations.[2] In other words, the controls are extended to terms which prevent the accrual of a promisor's obligation.

(ii) The Controls of the Act

Liability for negligence or breach of duty:

Clauses exempting a party from liability for his own negligence constituted a major source of injustice before the passing of the Act and was also the most difficult to justify on moral grounds.[3] On the whole, courts thought it "inherently improbable that one party to a contract should intend to absolve the other party from the consequences of the latter's own negligence"[4] and were, therefore, extremely reluctant

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1 Sections 13(1) and 25(3).

2 Sections 13(1) and 25(5). This provision applies only to sections 2, 5-7, 15, 16 and 19-21.

3 Joint Law Comm. op. cit., para. 44.

4 Gillespie Bros. & Co.Ltd. v. Roy Bowles Transport Ltd., Ronnie Hogg Ltd. [1973] Q.B.400, 419 per Buckley L.J.

to give effect to such clauses.[1] The Joint Law Commissions had considered the possibility of declaring all such exemption clauses void, but decided instead to subject them to a reasonableness test on the ground that such a clause might be justified where it would be more practical or economical for customers to insure themselves against loss or damage.[2]

The Act has followed this approach by providing[3] that a clause which limits or restricts a party's liability for loss or damage (other than for death or personal injury) occasioned by negligence or breach of duty, is subject to the reasonableness requirement. Negligence or breach of duty includes a breach - whether inadvertant or intentional and irrespective of whether the liability in respect of which arises directly or vicariously - of a duty to take reasonable care or exercise reasonable skill, whether express or implied under the contract or arising under common law.[4]

The different treatment of clauses excluding or restricting liability for death and personal injury and those exempting from liability for other loss or damage was suggested by the Joint Law Commissions, who thought it appropriate to attach greater importance to human life and person than to material goods.[5] However, unlike the Act, the Law Commissions were of the opinion that there might be

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1 See the strict rules of construction which the courts developed in order to limit the effectiveness of such clauses, ante, 251 et seq.

2 Op. cit., paras. 54-57.

3 Sections 2(2) and 16(1).

4 Sections 1(1) and 25(1).

5 Op. cit., para. 72.

situations where it was reasonable that the promisee took upon himself the duty to insure against death or injury and that clauses exempting from liability for such loss should be banned only where a party of weak bargaining strength relied greatly for his personal safety on the skill of the other.[1]

Contractual liability:

Both section 3 and the corresponding provision in Part II, section 17, apply in two situations: firstly, where one party is dealing in the course of business and the other not, and secondly, where one party is dealing on the other's "written standard terms of business" or where the contract is a "standard form of contract". In the latter setting protection is extended even to a party acting in the course of a business. The Law Commissions felt that to impose the controls on all contracts where both parties act in the course of a business would infringe too greatly on freedom of contract. It was, nevertheless, thought proper to give protection to a party acting in the course of business who had to submit to another's standard terms and who might have insufficient bargaining strength to prevent the inclusion of unreasonable terms.[2] Although the Commissions' proposal to extend protection to non-consumers was much criticised at the time it is submitted that it was realistic and its inclusion in the Act justified: a businessman may, because of particular contingencies, such as the financial difficulty of his business, be in as vulnerable a position as a consumer.

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1 Ibid., para. 74.

2 Ibid., para. 147.

In terms of sections 3(2)(a) and 17(1)(a) a party in breach may not exclude or restrict his liability for such a breach by a contract term unless it is reasonable to do so. The Law Commissions gave two examples of the exemption clauses which they wished to subject to control: (a) a provision that a carrier shall not be liable for loss unless it is reported to him in writing within seven days after delivery, and (b) a term in a builder's contract to the effect that liability for late delivery shall not exceed £X.[1] The injustice in such clauses lies in the fact that a promisor combines an apparently unqualified undertaking with a clause which excludes liability for failure to render proper performance. The unfairness is further compounded by the fact that the promisee, when he assesses the value of the contract does not normally contemplate a breach and does, therefore, not take account of provisions dealing with breach.[2]

A reasonableness requirement has also been imposed on a term which enables a party, in respect of a contractual obligation, to render no performance[3] or to render a performance which is substantially different from that which the consumer or customer reasonably expected from the contract.[4] These provisions deal with the situation where the terms of the contract imposes obligations on the promisor, but at the same time gives him such a wide discretion that he is more or less free to perform or not.[5] The protection of the Act applies even where a

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1 Ibid., para. 141.

2 Ibid.

3 Sections 3(2)(b)(ii) and 17(1)(b).

4 Sections 3(2)(b)(i) and 17(1)(b).

5 For example, where performance is made "subject to strikes" which, in fact, occur.

term defines a party's obligation rather than restrict his liability for breach.[1] Indeed, one of the main considerations of the Law Commissions in recommending these provisions was the fact that a clause may be drafted in such a way that technically it is not an exemption of liability at all.[2] It was clearly felt that such clauses which define and limit a party's obligation may mislead the promisee about the extent of the promisor's obligations and even where he does appreciate their effect, he may not have the bargaining strength to negotiate a material variation of the terms.[3] Although the traditional judicial techniques of strict construction and fundamental breach may have ameliorated the effect of exemption clauses they are not suitable tools for dealing with clauses which limited the promisor's obligation.[4]

The provision relating to the rendering of substantially different performance is potentially the most significant in the Act. Because account is taken of the reasonable expectations of the consumer or customer the other will not be able to cut down his obligations by careful drafting.

This approach is wholly justified and has in the U.S.A. been applied for a long time in respect of insurance contracts. According to Kessler

> /I/n dealing with standardized contracts courts have to determine what the weaker contracting party could legitimately expect by way of services according to the enterpriser's 'calling', and to what extent the stronger party disappointed reasonable expectations based on the typical life situation.[5]

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1 See, for example, the facts of Anglo-Continental Holidays Ltd. v. Typaldos Lines (London) Ltd. /1967/ 2 Ll.Rep.61.

2 Op. cit., para. 143.

3 Ibid.

4 See, for example, Anglo-Continental Holidays Ltd. v. Typaldos Lines (London) Ltd. /1967/ 2 Ll.Rep. 61, 67 per Russell L.J.

5 F. Kessler, Contracts of Adhesion - Some Thoughts about Freedom of Contract (1943) 43 Col.L.Rev. 629, 637. See also K.N. Llewellyn, Book Review (1939) 52 Harv.L.Rev. 700, 704.

Although Kessler limited his discussion to standardized contracts there is nothing to prevent a similar analysis being applied to contracts which, although formally negotiated, exhibit a similar tension between the core duties implicit in a specific type of contract and the ancillary terms.[1] The subject matter of this provision is not limited to exemption clauses, but may extend to any term of the contract. In determining whether performance is inconsistent with the reasonable expectations of a party the court will presumably have recourse to all the circumstances concerning the contract, for example, the reasonableness of the term, the opportunities for changing any standard terms, the comprehensibility of the wording of the contract, the opportunities provided to read the terms, whether such terms are often included in the particular type of contract, the extent of negotiation about the terms, and the representations made at the formation of the contract.[2]

Sections 4 and 18 apply only to consumer contracts and extend the requirement of reasonableness to any term which obliges the consumer to indemnify the other party for any liability of his to third parties in respect of his negligence or breach of duty or of his breach of contract. Such a clause will presumably seldom be held reasonable as against a consumer, if only because it will generally be easier for the business party to insure against such liability. However, in Gillespie Bros & Co.Ltd. v. Roy Bowles Transport Ltd., Ronnie Hogg Ltd.,[3]

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1 M.P. Ellinghaus, In Defense of Unconscionability (1969) 78 Yale L.J. 757, 796 footnote 177.

2 Reynolds, op. cit., 205.

3 [1973] Q.B. 400, 416-417.

Lord Denning thought that such a clause between two business parties was reasonable.

Sale of goods, hire-purchase and related contracts:

In terms of the Supply of Goods (Implied Terms) Act 1973, the same statutory undertakings are implied into sale of goods and hire-purchase contracts.[1] The Act also placed certain restrictions on the power of a seller or owner to limit his liability for breach of these undertakings: exemption clauses relating to the implied terms as to title are void,[2] and those relating to implied terms as to conformity with description or sample, quality or fitness for purpose are void in the case of consumer sales and hire-purchase contracts, but subject to a reasonableness test in the case of other sales or hire-purchase contracts.[3] These provisions have been re-enacted in, and made subject to, the reasonableness test as formulated in the 1977 Act.[4]

The Joint Law Commissions[5] felt that a similar system of control should be applied to other contracts under which ownership or possession of goods pass such as exchange, hire of goods and, in English law, the contract for work and materials, not only because they resembled sales and hire-purchase contracts, but also because of the possibility that the provisions of the 1973 Act might be evaded by

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1 Sections 12-15 of the Sale of Goods Act 1892 as amended by the Supply of Goods (Implied Terms) Act 1973 and sections 8-11 of the latter Act.

2 Sections 55(3) of the amended Sale of Goods Act 1893 and 12(2) of the Supply of Goods (Implied Terms) Act 1973.

3 Sections 55(4) of the amended Sale of Goods Act 1893 and 12(3) of the Supply of Goods (Implied Terms) Act 1973.

4 Sections 6 and 20.

5 Op. cit., paras. 13-27.

framing the agreements as something other than sales or hire-purchases. Such a system of control was accordingly introduced in sections 7 and 21. The Act does not purport to imply any terms into such contracts but refers only to those terms which are implied "by law from the nature of the contract". The controls contained in the Act do not, therefore, apply to terms implied other than by law or to express terms regulating the same subject-matter. As against a non-consumer a supplier can only exclude liability for breach of his implied obligations as to title, correspondence with description or sample, quality or fitness for purpose, if it is reasonable to do so. Unlike the provisions relating to sales and hire-purchase contracts the 1977 Act does not render void terms in this type of contract which exempt a supplier from liability for breach of the implied undertaking that he has the right to transfer or supply the goods. There may be cases where it will be reasonable to transfer goods even if the supplier only has a limited title to them, for example, where the transfer is only temporary.

(iii) The Reasonableness requirement

The centre of the Unfair Contract Terms Act is the reasonableness test, and the success of the Act will largely depend on the manner in which the courts administer this test. There is a difference between the ways in which the test is formulated in Part I and Part II. According to Part I the provisions subject to the test will be ineffective "except in so far as"[1] or effective "only in so far as"[2] they

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1 Sections 2(2), 3(2), 4(1) and 7(4).

2 Sections 6(3) and 7(3).

comply with the reasonableness test. Part II provides that similar provisions will have no effect if it was not fair and reasonable to incorporate them in the contract.[1] Although it is thus possible under Part I to hold a clause partly effective and partly ineffective it is doubtful whether there will, in practice, be many cases in which such a finding will be made.

There was disagreement between the Law Commission and the Scottish Law Commission as to the time at which the reasonableness test should be applied.[2] The latter was of the opinion that regard should be had only to the circumstances which were, or ought reasonably to have been, known to or in the contemplation of the parties at the time the contract was made. It was thought that to provide otherwise would be contrary to the normal practice and would create unacceptable uncertainty as to the extent of each party's rights and obligations with the result that a rational allocation of risks would be impossible to make. In the event, the legislature accepted the recommendation of the Scottish Law Commission.[3] However, there is considerable force in the proposition of the Law Commission that because the controls deal with unreasonable defences rather than unreasonable terms regard should be had to circumstances which actually occurred after the conclusion of the contract.[4] It is submitted that in

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1 Section 24(1).

2 Op. cit., paras. 170-182.

3 Sections 11(1) and 24(1).

4 Op. cit., para. 179.

practice the courts will, by holding that the parties ought to have known of certain circumstances, be able to judge the reasonableness of a term with some hindsight.

The reasonableness test proposed in section 3 of the Misrepresentation Act 1967 was criticised primarily because the standard was said to be so undefined that its application would lead to uncertainty. When a similar test was introduced in the Supply of Goods (Implied Terms) Act 1973, the legislature accordingly provided a number of guidelines for the application of the provision. These have been substantially reproduced in Schedule 2 of the 1977 Act for those transactions, and extended also to the analogous transactions covered by sections 7 and 21 respectively, and read as follows:

> (a) the strength of the bargaining positions of the parties relative to each other, taking into account (among other things) alternative means by which the customer's requirements could have been met.[1]

The question of whether inequality of bargaining power exists will be affected by the promisee's knowledge or presumed knowledge that he could have contracted elsewhere without having to agree to an exemption clause, his experience in transactions of the kind under scrutiny and the presence or absence of independent advice.[2]

> (b) whether the customer received an inducement to agree to the term, or in accepting it had an opportunity of entering into a similar contract with other persons, but without having to accept a similar term;[3]

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1 Cf. Levison v. Patent Steam Carpet Cleaning Co.Ltd. [1977] 3 W.L.R. 90.

2 Joint Law Comm., op. cit., para. 189.

3 Cf. Peek v. North Staffordshire Railway Co. (1863) 10 H.L.C. 473.

(c) whether the customer knew or ought reasonably to have known of the existence and extent of the term (having regard, among other things, to any custom of the trade and any previous course of dealing between the parties);[1]

(d) where the term excludes or restricts any relevant liability if some condition is not complied with, whether it was reasonable at the time of the contract to expect that compliance with that condition would be practicable;

(e) whether the goods were manufactured, processed or adapted to the special order of the customer.[2]

The Law Commissions were unwilling to provide guidelines for the application of the reasonableness test in respect of other contracts lest they should restrict the range of the factors to which the courts have recourse. However, it is likely that the guidelines supplied in Schedule 2 will be taken into account in all cases where the reasonableness test is applied.

The Act itself lays down two guidelines for determining the reasonableness of terms which restrict liability to a specific sum of money: regard must be had to the resources which the party seeking to rely on the clause could expect to be available to him for the purpose of meeting the liability should it arise, and the extent to which he could cover himself by insurance.[3] It is thought that these provisions refer to the situation where it is not possible to obtain insurance cover great enough to meet the liability which may be foreseen or where the cost of the insurance is disproportionately

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1 Cf. British Crane Hire v. Ipswich Plant Hire [1975] Q.B. 303; Grayston Plant v. Plean Precast 1976 S.C. 206.

2 Cf. Harbutt's "Plasticine", Ltd. v. Wayne Tank and Pump Co.Ltd. [1970] 1 Q.B. 447.

3 Sections 11(4) and 24(3).

high. The intention was, in particular, to cushion the effect of the liability on parties with limited resources. The onus of showing that a term is reasonable rests on the party who claims that it is.[1]

The reasonableness test under the 1973 Act has been applied only in Rasbora Ltd. v. J.C.L. Marine Ltd.[2] There it was held that a clause limiting to a short time period a boat-builder's liability to repair or replace items which were defective, was unreasonable.

The Law Commissions seem largely to have taken the view that the purpose of the reasonableness requirement was less to provide substantive justice inter partes than to provide a corrective to inequality of bargaining power, in so far as that is possible, so that the market may operate without distortions. If their endorsement of the practice developed under the Railway and Canal Traffic Act is an indication of future application of the reasonableness test the Act will provide little threat to contracts which are concluded under choice, however limited, and which are commercially justified. Nevertheless, the Act should obviate the need for conscious misconstruction by the courts in order to avoid giving effect to unfair clauses.

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1 Sections 11(5) and 24(4).

2 [1977] 1 Ll.Rep. 645.

PART III

EVALUATION AND CONCLUSION

The foregoing survey was intended to demonstrate that the courts have over a period of more than three centuries, frequently intervened in contracts because of a recognition -albeit often unarticulated - of the substantively unfair features of the transactions before them. Between the late seventeenth century and the present, the judicial approach towards unfair contracts has gone through roughly four phases of development.[1]

(1) 1675-1800

Seventeenth and eighteenth century lawyers, unlike their nineteenth century counterparts, did not conceive of private autonomy as an all-pervading ethic. While the courts recognised a sphere of private autonomy in contract law they were at the same time not reluctant to intervene in order to enforce the moral norms of the community. A whole system of controls arose, the effect of which was to enforce a standard of equivalence in the values exchanged. This standard, which derived from the doctrine of usury, found expression in two distinct forms of control, which can respectively be described as "paternalistic" and "regulative".[2]

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1 These phases are not watertight compartments. The classification adopted serves to illustrate general trends in judicial attitude and does not suggest that conflicting decisions do not exist.

2 The terms "paternalistic" and "regulative" are derived from D. Kennedy, Form and Substance in Private Law Adjudication (1976) 89 Harv. L. Rev. 1685, 1735-1736. In adopting these terms to describe the forms which judicial action can take I have not necessarily adhered to the meanings which Kennedy assigned to them.

In the case of paternalistic control the standard of fair exchange was enforced through the principle that the function of contract is compensatory, not punitive. All contract terms which violated this principle were set aside, without reference to the circumstances in which the contract was entered into. Although intervention might initially have been motivated by circumstances external to the contract terms, such as the respective positions of the parties, the test subsequently applied was objective and aimed solely at establishing whether or not a term had infringed the fundamental nature of contract as a compensatory mechanism. Examples of this form of control were the doctrines against forfeitures, penalties and penal irritancies.

In other areas the role of the courts was circumscribed by the realization that too strict an insistence on equal exchange would lead to commercial stagnation. The control exercised by the courts was therefore confined to exceptional cases. The function of regulative control was to detect and correct those factors which distorted the normal bargaining process. Of these factors the most significant were those relating to the condition of and relationship between the parties. Although neither Scots nor English law ever accepted a doctrine as inflexible as laesio enormis the cases clearly indicate that relief was granted from a bargain transaction where a gross disparity in the values exchanged could be explained by a bargaining handicap in the disadvantaged party. This form of control was exercised mainly through instruments like fraud, which, because of their width and undefined character, enabled the courts to take into account all the circumstances of the case before them.

(2) 1800-1870

The rise of the classical theory of contract in the nineteenth century resulted in the reformulation of contract principles so as to express the individualistic premise on which not only law, but also politics and economics were then based. In terms of this theory the highest good to the community would follow from a judicious and enlightened seeking of self-interest and the only task of the courts was to protect a party's free will. Justice was to be done by adhering to the principle of freedom of contract and not by pursuing an objective of individualized justice through external regulation.

The main effect of the new doctrine was the scaling down of the wide, undefined remedies like fraud and bona fides to clearly circumscribed and more limited proportions: a system in terms of which justice would follow from a strict application of general principles could not allow the existence of discretionary judicial powers of intervention. In addition, the function of the judicial remedies which remained was redefined so as to accord more closely with the fundamental aim, not of regulating unfair transactions, but of protecting the freedom of the individual will.

However, the practice of the courts was not as monolithic as the prevailing dogma. In England the Chancery courts continued to give relief from unfair contracts on the ground of equitable fraud, and also extended the scope of relievable coercion. And although the Scots law concept of fraud was severely whittled down, regulative control was still exercised on a limited scale through facility and circumvention and occasionally through extortion. By the mid-nineteenth century the full implications of freedom of contract had not yet infiltrated into all areas of contract law.

(3) 1870-1945

The strictest judicial adherence to freedom of contract occurred in the late nineteenth and early twentieth centuries. In English law one of the main reasons for the increased rigidity was the fusion of common law and equity in the 1870s. The result was the virtual eclipse of equity as a residual system of discretionary justice and the consequent disappearance of many of the protective doctrines developed by the Chancery courts. As a result of the restricted role assigned to the courts, instances of regulative control were limited to an absolute minimum and earlier examples of paternalistic control were ascribed to the supposed intention of the parties rather than to judicial lawmaking. In Scots law a similar contraction in the scope of judicial control took place, a process which was exacerbated by the increasing tendency to rely on English decisions for guidance.

Paradoxically, all this was occurring at a time when in the political and economic spheres the virtues of individualism were beginning to be questioned and when interventionism was again gaining respectability. The assimilation of these ideas by the courts was slow and limited, but it did, especially in the twentieth century, cause a subtle change in judicial attitude: whereas some earlier courts had shrugged off individual cases of hardship as the price which inevitably had to be paid for the long-term good of the community there was then an increasing recognition of and concern about the substantive unfairness in contracts. This shift in attitude was further impelled by the increasing use of standard form contracts. But although the courts were prepared to recognise that the exclusive power of one party to prescribe the terms of the transaction was

frequently abused, they were constrained from exercising direct control by the classical notion that the courts should not police substantive unfairness in contracts. Control of unfair contracts was, therefore, exercised indirectly, by manipulating the rules of consent and interpretation. The courts, unable to conceive of contracts otherwise than in terms of the classical model with its implicit assumption of individualized bargaining, lacked the perspective needed to deal effectively with the problem of unfair standard form contracts.

Whereas in the previous era relief from unfair bargains was refused because individual cases of unfairness were regarded as irrelevant in principle, in this phase direct control was refused because the courts, it was said, did not have the power to control the substantive fairness of contracts. In areas where hardship occurred frequently it was left to the legislature to confer on the courts such powers of intervention.

(4) 1945 -

The picture which emerges from the last thirty-five years is a conflicting one. On the one hand, the trend away from the precepts of classical individualism, already evident in the previous era, has strengthened in contract law as it has in the fields of politics and economics.

Apart from the general loss of confidence in individualism, the most significant factor contributing to the decline of freedom of contract has been the rise of the standardized contract to being the norm rather than the exception. Two characteristics of standard form

contracts caught the attention of the courts: firstly, the fact that there was no individualized negotiation about the terms and that parties often agreed to them unread or unseen, and secondly, that standardized contracts are employed mostly by commercial enterprises which often have greater economic power, information, expertise and experience than the counterparty, who is required to assent to the terms in toto. Standard form contracts again brought to the fore the relative position of the parties. This has led not only to attempts by the legislature and the courts to redress the balance by recognising the special interest of the consumer, but also to an increased focus on the respective positions of the parties even outside the sphere of the consumer-merchant relation. All these developments involved the court in a closer scrutiny of the facts of the particular case and thus constituted a movement away from generalised justice attained through the application of freedom of contract.

The insights gained by the courts in the sphere of standard form contracts have resulted in a greater willingness to control substantively unfair contracts generally: the discretionary power of control has been re-affirmed in the sphere of forfeitures, the doctrines of duress, force and fear and restraint of trade have been extended, the rules of consent have been further tightened up, the substantive doctrine of fundamental breach restricted the effectiveness of exemption clauses, unfair contracts traceable to the exploitation of a bargaining handicap have been set aside in a few cases and legislation subjecting exemption clauses to a reasonableness test has been introduced.

On the other hand, although there has been a growing consensus that control over contract terms is sometimes necessary, there is, at the same time, a continuing reluctance on the part of some judges to admit that to do justice in a particular case is a legitimate judicial pursuit. The tendency is therefore to interpret those instances where judicial control takes place as exceptions to the principle of freedom of contract rather than as part of a fundamental reassertion of the courts' role in marking out the boundaries beyond which contractual terms become unacceptable.

The controls exercised in modern law do not present a systematic and co-ordinated response to the problem of substantive unfairness in contracts. The techniques employed are the products of different philosophical backgrounds and often unconnected lines of development originating from distinct sources. As a result of the ambivalent judicial attitude towards the controlling function these techniques have developed largely in isolation with little interchange of ideas amongst them, and, consequently, with no emergence of any organising principle to bind together the judicial remedies into a coherent system of controls. In addition, although the peculiar nature of standardized contracts has been fully diagnosed there has been an inability to adapt the conventional contract rules so as to deal more effectively with unfair terms which are unilaterally prescribed. Legislative intervention has been confined to specific areas of concern such as credit transactions and exemption clauses. All these factors have contributed to making the present control of unfair contracts confused, inconsistent and often ineffective. This situation can only be remedied if there is consensus about the degree and range of judicial action

and about the premise upon which judicial control should proceed.

Comment

(a) The range of judicial action

Judicial action should have only a limited objective. As the courts do not have the wherewithal to restructure inequalities which are inherent in the social and economic system they should not attempt to redistribute wealth and economic power.[1] While the courts might outlaw certain contractual terms by reference only to their nature and effect, they should not, in exercising regulative control, take account of the basic inequalities between the parties: for example, a court might set aside an unfair contract on the ground that it resulted from the exploitation of a specific bargaining handicap of a party, but it should not assume that contractual terms resulted from the exercise of unequal bargaining power merely because there existed an institutionalised inequality between the parties, such as between a composer wishing to publish his songs and a publisher. To establish the necessary causal link between an unfair term and the exercise of institutionalised unequal bargaining power would, in the absence of monopolistic conditions, involve the court in a wide-ranging inquiry into economic questions which it is not qualified to undertake. Regulative judicial control should, therefore, be confined to those cases where the determination of causation lies within the practical capability of the courts.

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1 See, generally, A. Schwartz, Seller Unequal Bargaining Power and the Judicial Process (1974) 49 Ind.L.J.367; J.P. Dawson, Economic Duress - An Essay in Perspective (1947) 45 Mich.L.Rev. 253, 289; R.L. Hale, Bargaining, Duress and Economic Liberty (1943) Col.L.Rev. 603, 624.

(b) The premise upon which control should proceed

Attempts have recently been made to supply an organising principle or central premise underlying the various heads of control. Lord Denning has suggested that inequality of bargaining power is the common thread which runs through the various remedies,[1] and other commentators have suggested a synthesis of the various protective doctrines under the head of economic duress.[2] In my view these principles do not provide an adequate explanation of all the controls exercised. Furthermore, by formulating the central principle in non-substantive terms the main focus of the inquiry is again diverted from the content of the contract.

Although it is difficult to postulate a single proposition underlying controls as diverse as those examined, I believe, and have attempted to demonstrate, that most instances of intervention proceed from the premise, albeit often unexpressed, that the contract under scrutiny is substantively unfair. And if there is to be consistency in the control exercised the courts must either assume a general power to police substantive unfairness in contracts or it must be conferred by legislation. Only then can the courts build up a coherent system of controls. Postulating substantive unfairness as the underlying premise of judicial control does not mean that relief should be

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1 Lloyds Bank Ltd. v. Bundy [1975] 1 Q.B. 326, 336-339.

2 See, J. Dalzell, Duress by Economic Pressure (1942) 20 N.C.L. Rev. 237, 341; F. Wooldridge, Inequality of Bargaining Power in Contract (1977) J.B.L. 312.

granted from every contract which is one-sided or which stipulates for an unequal exchange. To do so would place too great a limitation on commercial activity. The task of the courts must, therefore, be to identify those circumstances which will, together with substantive inequitability, provide a sufficient ground for relief. There can be no single such test of unfairness which is applicable to all contracts and all factual settings. Judicial control of unfair contracts must proceed through the recognition and classification of different type situations and the establishment of various "models" of unfairness, unconscionability or unreasonableness. It is clear, especially from the practice in the seventeenth and eighteenth centuries, that this is a task which the courts are qualified to carry out.

The two most basic type situations which should be identified and isolated for separate treatment are unfairness arising in the context of negotiated contracts and that which occurs in the sphere of standard form contracts.

(i) Standard form contracts

The standardized transaction has become the most common context in which instances of substantive unfairness are found. This is not only because the vast majority of contracts entered into are now in standard form, but also because the terms of these contracts are, by the very nature of these transactions, not fixed by negotiation between the parties. Standard form contracts are depersonalised mass transactions, drafted by one party and presented for acceptance to a variety of counterparties without taking into account their particular circumstances and characteristics and often without intending the terms, other than those which embody the core of the transaction, to be

specifically scrutinised or understood.

This manner of contracting has great advantages, not the least of these being that they facilitate a rational regulation of legal risk. At the same time, the fact that one party has the exclusive power to draw up the terms on which he is prepared to contract has led to such contracts being drafted in a one-sided manner and with disregard to the interests of the offeree. Quite correctly, the courts have felt the need for control where the terms are grossly imbalanced. However, with a few exceptions, these controls have been exercised either instinctively as in the case of strict construction or by manipulating contract rules which were developed on the assumption of individualized negotiation. Clearly, these techniques are unsuitable for dealing with unfairness in contracts which are by definition mass, and not individualized transactions.

Recently some courts have purported to control unfair standard terms by reference to unequal bargaining power.[1] This approach is also unacceptable. Where the nature of the contract itself precludes any bargaining about the terms it is surely inappropriate to base relief on the impairment of one party's bargaining power. The only form of inequality of bargaining power which is relevant in the context of standard form contracts is that which arises from the market structure and, as I have argued before, to establish a causal link between such inequality and a specific term in a mass contract involves

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1 A. Schroeder Music Publishing Co. v. Macaulay [1974] 1 W.L.R. 1308; Clifford Davis Management Ltd. v. W.E.A. Records Ltd. [1974] 1 W.L.R. 61.

the court in an inquiry so wide-ranging and of such complexity as to make inequality of bargaining power unsuitable as a criterium for relief in litigation where the complaining party will generally be a private individual.

Instead, it is suggested that as standard form contracts are by nature depersonalised, the test whether a contract is fair should largely be confined to the terms themselves and individualized questions such as those relating to the knowledge which the offeree had of the terms or the inequality of the parties should be excised from the court's enquiry. At most, the courts should take into account the broad type of contracting party to whom the standard form is usually offered, for example whether they are consumers or businessmen. The role of the court is, therefore, to exercise paternalistic and not regulative control and its task is to mark out, in accordance with the standards of the community, the limits beyond which certain contractual terms will not be tolerated.

In deciding whether a contract is fair or not the court should take into account the commercial reasonableness of the terms, but even so, it should not allow those which are clearly outrageous or which are inserted only to harass or mislead the counterparty. To a large extent the question of fairness must depend upon the type of transaction involved. As the fairness of a standardized contract is not to be judged by reference to the quality of consent or the relative positions of the parties the courts' task is to develop techniques for the

> marking out for any given type of transaction what the <u>minimum decencies</u> are which a court will insist upon as

> essential to an enforceable bargain of a given type, or as being inherent in a bargain of that type.[1]

According to Llewellyn "/t/he picture is one of this or that transaction-type as having ... an essence which contains a minimum of balance, a core without which the type fails of being."[2]

This approach to unfair contracts is not new. It has long been followed in German law in respect of standard form contracts[3] and in English and Scots law it has a precedent in the seventeenth and eighteenth century treatment of forfeitures, penalties and irritancies which infringed the fundamental nature of contract as a compensatory mechanism and more recently in the substantive doctrine of fundamental breach. A tool through which such delimiting of the "iron essence" of each transaction type can be effected has now been supplied by the provision in the Unfair Contract Terms Act 1977 which subjects to a reasonableness test all terms which enable a party to render performance substantially different from that expected of him.[4]

(ii) Negotiated contracts

The control of unfairness in the context of negotiated bargains must, just as in the sphere of standard form contracts, proceed by way of recognition and classification of type-situations, both as regards factual settings and remedies. One of the most important models of

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1 K.N. Llewellyn, Book Review (1939) 52 Harv.L.Rev. 700, 703.

2 The Common Law Tradition, 368.

3 J.P. Dawson, Unconscionable Coercion - The German Version (1976) 89 Harv. L.Rev. 1040, 1103-1126.

4 Sections 3 and 17.

unfairness occurs where a grossly unfair exchange is produced by the exploitation of a bargaining handicap - physical or mental disability, a wide disparity of knowledge and experience, and economic necessity - existing in one party. Relief in these circumstances, although it has fallen into desuetude, was well-known in both English and Scots law in the seventeenth, eighteenth and even in the nineteenth centuries. Lord Denning's recent resurrection of the doctrine in the guise of "the principle of inequality of bargaining power"[1] is thus based on firm precedent. Although no similar advances have been made in modern Scots law the Scottish Law Commission[2] has suggested the recognition of a category of "lesion" in terms of which relief will be given where a party can show that an unfair advantage has been taken - that is when there is a gross disproportion between the respective exchanges or when a serious prejudice has been or will be sustained - of his weak personal or economic position.

Whereas the Scottish Law Commission proposed lesion as a substitute for facility and circumvention, extortion and undue influence, but not for force and fear, the place of Lord Denning's principle of inequality of bargaining power in the fabric of controls is uncertain. Although the principle was said to derive from duress of goods, the doctrines of undue pressure, undue influence and the relief granted from unconscionable bargains in equity and unfair salvage agreements, it is not clear whether it merely supplements these or is a substitute

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1 Lloyds Bank Ltd. v. Bundy /1975/ 1 Q.B. 326.

2 Memorandum No. 42: Defective Consent and Consequential Matters, paras. 3.129-3.131.

for them. In English law the distinction between the exploitation of a bargaining handicap and the exercise of coercion has, as a result of the very narrow interpretation of common law duress, never been very sharply defined. A strong case can therefore be made for the subsumption of the various categories of control enumerated by Lord Denning under either a principle of inequality of bargaining power or a liberal doctrine of economic duress. In Scots law, however, these abuses have always received distinct treatment.

The judicial exercise of a discretionary power of control over unfair contracts has limited effectiveness as a means of consumer protection. Litigation over transactions which may involve relatively limited amounts will be initiated only by a small number of private individuals. Yet, as a residual measure this form of control is of great importance. The development of an effective system of controls can, however, only take place if the courts openly recognise that judicial control of unfair contracts has always taken place, that the fairness of a contract is a legitimate judicial concern, and if there is agreement as to the system of values upon which control is to be based.

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